Overseas Asset Management

Overseas Asset Management (Cayman) Ltd.
The Pavilion Cricket Square
PO Box 597 Grand Cayman KY1-1107 Cayman Islands
T 345 949 8787 345 949 8780 F 345 949 7760
E info@oam.com.ky www.oam.com.ky

OAM European Value Fund

9th January, 2018

Dear Fellow Shareholder,

2017 was one of our better years. I am inclined to remind myself of the saying: don't confuse brains with a bull market.

In last year's Chairman's statement, I wrote:

> "At the start of 2013, we updated the Fund's prospectus and set a new absolute return objective which was to provide shareholders with returns over the next ten years at least five times higher than the yield on 10-year United States Treasury bonds, i.e. at least 8.75% per annum for 10 years. This implies a target NAV of at least $77.50 in six years. That target is looking very ambitious, but if currency moves in our favour by around 5% per annum, it remains a realistic target. Although the Fund's NAV has only increased by 4.4% per annum in US Dollars since we set this target 4 years ago, it is worth noting that the return in euros is 10.5% per annum. This illustrates the importance of currency in determining returns."

In 2017, the Fund's NAV per share increased by 31.3% compared with an increase in its benchmark, the MSCI Europe (US$) index, of 21.9%. Currency played an important part in boosting returns. During the year, the euro appreciated 14% against the US Dollar and even Sterling, the most hated currency in the developed world, rose by 10% last year against the Dollar. With a currency tailwind for a change, the above target seems easier to achieve. It implies an 8% annual return over the next five years. During the first 15 years of the Fund's life, its NAV/share compounded at 11.6% per annum. By comparison, the Fund's benchmark rose by 4.8% per annum. The benchmark figures used for comparison do not include dividends. We estimate that if dividends, net of withholding taxes, are included in the benchmark returns, they would increase by around three percentage points.

Currency

The way we view currencies, and equity markets, is that their valuation swings like a pendulum from overvalued, through fair value, and on to undervalued, before swinging back to fair value. It is far from the perfect predictable pattern of a real pendulum, but to paraphrase some wise wit, imagine how hard physics would be if electrons had feelings! In the real world where the emotions of investors and speculators come into play, the pattern is far from symmetrical, but there is a strong discernible pull like gravity back to fair value that becomes more powerful the further prices or exchange rates stray from fair value, leading to sharp corrections at extremes. Last year, I stated that our estimate of fair value for the euro was 1.25, and

for sterling it was 1.50. I also cited an empirical study which showed that 5-year periods of strong returns for the US Dollar are almost always followed by 5 years of negative returns for the US Dollar index, and vice versa. During the 5 years ending in December 2016, the US Dollar index strengthened by more than 5% per annum.

A year ago, it felt as if the views of investors and speculators had become very polarised in favour of further US Dollar appreciation. In December 2016, the Economist graced its cover with a picture of George Washington flexing his muscles and the title "The Mighty Dollar". I do not mean to pick on the Economist – we are a subscriber – but their covers often portray consensus, polarised views of markets near market peaks or troughs when sentiment is very one-sided. For instance, a March 1999 cover of The Economist was published when the price of oil was $13/barrel. Although it suggested that the world was "drowning in oil", over the next 9 years, the price of oil increased more than ten-fold. Likewise, a November 2009 Economist cover suggested that Brazil was about to take off. Over the next 6 years, Brazilian equities in US$ lost 75%.

The euro, in particular, has snapped back against the Dollar in the past year, but it still looks undervalued. Sterling looks even cheaper.

<u>Value vs Growth</u>

Last year, I said that I thought the cycle of value stocks underperforming growth stocks had finally turned and is now firmly behind us. As this chart of the MSCI Europe Value Index relative to the MSCI Europe Growth Index shows, this has not yet happened.

In reviewing our past performance, we think it adds insight if we split the Fund's history into two periods: the first five years from 2003-2007, and the nine years from 2008-16. During the first period, the Fund's NAV per share more than tripled, compounding at 27% per annum during those five years. During the second period, the Fund's NAV per share only increased by 20%, compounding at 2% per annum during those nine years. During the first period we had three factors in our favour: currency appreciation, an equity market revaluation, and European value stocks outperforming growth stocks. During the following nine years, all three factors went into reverse and provided a strong headwind to returns. As the following table shows, European exchange rates, European equity market valuations, and the valuation of European value stocks relative to growth stocks were all lower at the end of 2016 than at the Fund's launch at the end of 2002.

Two distinct periods: 2003-7 & 2008-16

As at 31 December	2002	2007	2016
EUR/USD	1.05	1.46	1.05
GBP/USD	1.61	1.99	1.23
Price/Book MSCI Europe	1.8	2.2	1.7
P/B Value discount vs Growth	-58%	-46%	-63%
OAM European Value Fund NAV	$ 10.00	$ 33.24	$ 39.79

This reversed slightly in 2017. Currency and valuation recovered slightly, but European value stocks did not outperform growth stocks. We think there is likely to be more reversal to come over the next few years from these three factors. If we are right, they should provide a tailwind to returns.

Greater portfolio concentration

At year end, the Fund had 42 investments if we count different classes of shares in the same company as one, or different listed components of the same group as one. The 15 largest holdings account for more than half the Fund's net assets; the next 10 largest for more than 20% of net assets; and the remaining 17 holdings for only 8% of net assets. The remaining assets are in cash. Furthermore, many of these holdings are in clusters such as listed private equity funds, Italian holding companies, Russian companies with listings in London, banks and insurance companies, shipping, and agriculture. The portfolio is much more focused than it has been throughout most of its history, concentrating on industries that we both understand and where there are a number of listed companies that we think are currently trading at well below our estimate of intrinsic value. Since we are bottom-up investors, I will explain the investment rationale for our larger holdings or give an update where extensive commentary was provided in last year's Chairman's statement.

Listed private equity funds

Currently, the Fund has $40 million or 14% of the Fund's net assets invested in five listed private equity investments: Ashmore Global Opportunities, Altamir, Spice Private Equity, Pantheon International, and Better Capital 2009/2012. During the year, we sold NB Private Equity, generating an excellent return during our holding period. We had some reservations about the high yield portion of that fund's portfolio and its discount to NAV narrowed to a level that did not give us enough protection for the risks we perceived. We also received distributions (at net asset value) during the year of $1 million from Ashmore Global and $3.4 million from Better Capital 2009. We also initiated a new holding in Better Capital 2012. The table on the following page shows the Fund's current holdings in this sector.

Fund	Current value of investment	% of fund Owned	Share Price	NAV per Share	Discount to NAV
Ashmore Global	$12.2 million	28.0%	$3.80	$6.00	-37%
Spice PE	$7.7 million	5.0%	$28.90	$40.96	-29%
Altamir	$9.2 million	1.4%	€15.24	€21.05	-28%
Pantheon	$7.6 million	0.6%	£18.62	£22.21	-15%
Better Capital 2009	$0.6 million	0.4%	£0.60	£1.15	-48%
Better Capital 2012	$2.8 million	2.7%	£0.24	£0.45	-44%

The share price of Ashmore Global Opportunities Ltd. (AGOL) declined marginally during the year on thin volume to close the year at $3.80. This makes little sense. During the year, AGOL's NAV per share increased 19% to $6.00. Furthermore, AGOL repurchased 5% of its shares on a pro-rata basis at its NAV per share at the end of September. Consequently, the share price discount to NAV is 37%.

The three largest holdings in AGOL are Bedfordbury, Microvast and AEI. Bedfordbury, which accounts for 35% of net assets, owns a land bank on Manila Bay in the Philippines. Manila has a very small central business district (CBD) of only a few blocks and this land bank is on the edge of the CDB which desperately needs to be expanded. Hence, the land bank is very valuable and sought after. Ashmore is in a dispute with their Philippine partner which is being arbitrated in Singapore; the case has been delayed a few times and is now scheduled for the third quarter of this year. AGOL is carrying the land at what appears to be an attractive valuation. Microvast, which accounts for about 25% of AGOL's net assets, has so far delivered 5,000 electric buses in China and 800 in the U.K. CITIC injected $400 million into the company in February. AGOL marked up the value of this holding and the company is performing very well so further upside looks likely. The most likely exit for AGOL is through an IPO of Microvast.

AEI's only remaining asset is Jaguar Energy, a power plant in Guatemala, which accounts for about 17% of AGOL's net assets. An investment bank has been appointed to find a buyer. The next largest asset in AGOL is the head office and main distribution centre for DHL on the ring road around Moscow. The lease and rent is in USD, though it has been reduced following the ruble devaluation. It is being valued at an attractive rental yield. Ashmore seem quite confident that the remaining positions in AGOL can easily be sold within the next two years. We think that AGOL is likely to return most of its capital this year. If they return NAV, our upside will be over 50% or more than $7 million.

Spice Private Equity is managed by GP Investments, a leading Brazilian private equity fund manager. GP Investments has a strong alignment of interest with minority shareholders as GP owns 58.5% of Spice's shares. Spice's NAV per share performance is far more important to GP than management fees, giving a much stronger alignment of interest between the manager and shareholders than at most private equity funds. This is important in that it will likely prevent GP from overpaying for acquisitions in what is currently quite a hot market. Spice has $77 million in cash, a $37 million receivable from Blackstone following the sale of its legacy portfolio, and $104 million in investments. The largest of these investments is Leon, a fast food chain in the UK that serves healthy food and which is expanding rapidly and it accounts for nearly 15% of NAV. This investment was made in May. The second largest investment is in Rimini which sells enterprise

software support products and services. That investment was made in October alongside GP Investments and it accounts for 11% of NAV.

We engaged with the Board of Spice for more than a year and suggested that they repurchase shares, which they have started, albeit at a much slower pace than anticipated. During the year, I met with Board members of Spice who said that they think that Spice needs to make attractive investments, generate a strong NAV return, and get bigger so that the shares become more liquid before the wide discount to NAV can be tackled effectively. We are happy to give the Board and GP Investments five years from the change in strategy, which took place in June 2016, to prove whether their strategy is working. I suggested to the Board that if Spice's NAV is not much higher than where it was when the change in strategy came into effect ($42/share), then Spice should offer minority shareholders an opportunity to exit at close to NAV. Spice's directors assured us that they are reducing expenses and that the management fee will fall this year.

As I mentioned in last year's Chairman's statement, we have been urging Altamir to return capital to shareholders in a more tax efficient manner by repurchasing shares, rather than pay a dividend. It is now clear that Altamir will not heed to our request. Maurice Tchenio, a co-founder of Apax and Chairman of Altamir, owns 28% of the fund. This creates the same strong alignment of interest that we have with Spice. However, in respect of the dividend issue, our interests and Maurice's are not well aligned in this respect. As a French citizen, he receives the dividend free of any withholding tax. We, on the other hand, are levied at a 30% withholding tax rate, therefore losing more than 1% of the value of our investment each year through tax leakage.

Altamir is structured as a SCR, a type of company for which, according to the French Tax Code, there is no French withholding tax on dividends if the beneficiary is a legal entity having its registered office in a state that has signed a treaty with France containing an administrative assistance provision. We argued in an e-mail to the Director of the Cayman Department for International Tax Cooperation (DITC) and the Minister for Financial Services that there is a clear case for France not withholding tax on dividends for this type of French company on the basis that Cayman provides tax assistance (through a bi-lateral Tax Information Exchange Agreement (TIEA)) and will shortly be providing automatic exchange of tax information to French tax authorities (through the OECD's Common Reporting Standards (CRS)). The DITC followed up with the French Ministry of Finance who have since confirmed that our TIEA is treated in the same manner as a double taxation agreement (DTA) with administrative assistance/exchange of information provisions. Altamir was very helpful and had their tax counsel in Paris review the matter with the French authorities. In November, the French Ministry of Finance said that they do not expect to give an answer for about a year! In the meantime, the French Government recently reduced the withholding tax rate of dividends paid by French companies to non-French shareholders from 30% to 12.8% with effect from 1st January 2018. This is very good news for our French investments, particularly Altamir and Gaztransport et Technigaz, both of which pay generous dividends.

In 2015 and 2016, Altamir's NAV per share increased by nearly 20% in each year, a testament to its strong management. This past year, its NAV per share was essentially unchanged, with NAV growth taking what we expect to be a short-term breather from decent growth. Altamir's share price discount to NAV at 28% is much too wide for a top-tier fund.

Pantheon International merged its two classes of share into a single class during the past year which will improve liquidity in the shares, and hopefully help narrow the discount to NAV at which the shares trade. They continue to buy back shares at a discount to NAV which is accretive to its NAV per share. Last year, Pantheon increased its NAV per share by 6%.

Better Capital 2009 returned more than the value of this investment at the start of the year following the sale of Gardner Aerospace. We have been adding to Better Capital 2009, and during the year, we initiated a holding in Better Capital 2012. Jon Moulton, the founder of Better Capital, has been buying shares in both funds in the open market this past year which we find encouraging.

Financials

Our banks and insurance companies generated strong returns last year. Currently, the Fund has $58million or 21% of the Fund's net assets invested in six financials: Standard Chartered Bank, Sberbank, Close Brothers, NN Group, Vienna Insurance Group, and Hiscox. Banks and insurance companies typically benefit from an increase in interest rates, something that we regard as a near certainty in the medium term. Two of our banks and two of our insurance companies are in many respects turnaround situations at various stages of their recoveries. Sberbank is at the most advanced stage of its recovery. The bank was already very well-run, but a recovery in the Russian economy boosted earnings. During the year, earnings estimates for 2017 increased by 25%. The share price rose by 30% in rouble terms so very little of the return came from P/E revaluation. With appreciation in the still undervalued rouble and dividends, the total return for the year in Dollars was 52%. Sberbank's shares still look very undervalued as shown by the metrics in the table on the following page.

NN Group is next furthest along in its recovery under the able leadership of Lard Friese. During the year, NN Group completed its purchase of Delta Lloyd at what looks like an attractive price. Senior management has wrung out further cost savings and is starting to reap synergies from merging its business with Delta Lloyd in the Benelux markets. During the year, earnings estimates for this year increased by 50%. Some of these earnings increases were one-offs last year, but it still led to NN Group generating a return in Dollars last year of 34%. The shares still look undervalued and offer a free cash flow yield of more than 10%.

Vienna Insurance Group is probably the next furthest in its turnaround. Through further expansion into Eastern European markets, we expect it to generate a more respectable return on equity (ROE). The shares returned 42% last year in Dollars.

Standard Chartered is still at an early stage of its recovery. We believe that Bill Winters is doing all the right things and expect the shares to generate a very attractive return in the next 3-5 years. This is a fundamentally strong business with a valuable brand. Prior to the set-back from 2013-15 under different leadership, the bank generated a 17% compound annual return for shareholders over the 20 years from 1993-2012 compared to a 7% compound annual return for the FTSE All Share index over the same period.

Close Brothers is a very high quality business which generated a compound annual return of 15% per annum in sterling over the past 25 years. I mentioned in last year's Chairman's statement that "Close Brothers will see its EPS growth held back this year as its effective tax rate rises from 18.5% to 26% as the effect of the last UK Chancellor's bank tax surcharge kicks in." This tax surcharge caused Close Brothers to report an uncharacteristically small increase in earnings for the year ended 31st July 2017 of only 3%. This provided us with an opportunity to buy more shares at an attractive valuation of about 10 times estimated earnings and a 4.5% dividend yield.

Hiscox rounds out our financials. It is a superb insurance business and brand. They are excellent underwriters and were able to dodge the worst of the 2017 hurricane season and benefit from a rise in premium rates. The shares returned 61% in Dollars last year.

Company	Current value of investment	Price/Book	2017 P/E	Div yield	ROE
Standard Chartered	$9.8 million	0.7	n/m	-	n/m
Sberbank	$11.9 million	1.6	8	2%	20%
Close Brothers	$10.0 million	1.8	11	4%	16%
NN Group	$12.6 million	0.5	7	4%	6%
Vienna Insurance	$8.4 million	0.8	13	3%	6%
Hiscox	$5.4 million	2.2	17	2%	13%

European family holding companies

We have long been attracted to European family-controlled companies, particularly family-controlled holding companies trading at deep discounts to NAV. Historically, a lot of these were listed in Italy, France and Belgium. Today, the deepest discounted family-controlled holding companies that we own are Norwegian. This is in a sense an oddity given Norway's responsible fiscal management. In another sense, it is rational because as I mentioned in last year's Chairman's statement, Norwegian families have little incentive to narrow the discount to NAV at which shares in its listed companies trade because Norwegian residents who have a net worth of more than NOK 1.5 million must pay a wealth tax of 0.85% of the value of their net assets annually. In 2006, Sweden elected a right wing government and the following year, it eliminated its wealth tax. In September, Norway Conservative leader Erna Solberg was re-elected as Prime Minister following her pledge to reduce taxes. Elimination or a reduction in Norway's wealth tax is a possibility.

We have an investment now worth $10.5 million in Wilh. Wilhelmsen Holding ASA. The shares appreciated further last year and have doubled from where we bought them 2 years ago. I wrote extensively about this holding two years ago, so I will say little other than that we think the shares are still significantly undervalued, trading at a discount to NAV of about 45%. The shares also look cheap on 7 times consensus estimated earnings for 2018 and a dividend yield of 2%.

We also have an investment in the Olsen family holding company, Bonheur, currently worth $7.7 million that looks even more undervalued. We estimate that its Scottish and Scandanavian windfarms are worth about NOK 5.7 billion. About half of this value is attributable to its 51% interest in its Scottish wind farms business, FOWL, which they own with The Renewables Infrastructure Group Ltd. (TRIG), a London-listed closed-end fund, based on the price that TRIG paid for a non-controlling interest in FOWL. We attribute no value to its offshore wind concessions that are in the early stages of development. We estimate that its cash-rich cruise ship business which operates cruises from Britain and Scandinavia to be worth about NOK 1.8 billion. Bonheur also owns two ships that erect offshore wind turbines that we value at depreciated book value of NOK 1.4 billion. Bonheur also owns a controlling stake in the Norwegian-listed Fred Olsen Energy (FOE) which owns mid- and deep- water oil rigs. FOE's share price collapsed along with the price of oil over the past few years and this stake is now only worth NOK 0.7 billion. Bonheur also has net cash and other investments worth NOK 0.8 billion. The sum of the parts is over NOK 10 billion and Bonheur is valued at a 64% discount to its estimated NAV. Bonheur pays a regular annual dividend so we are paid while we wait

for the discount to NAV to narrow. Meanwhile, we have two possible catalysts: a recovery in FOE if the oil price recovers, and further development of the windfarm business using its ample cash from the sale of 49% of FOWL to TRIG in 2015. It is apparent that the Olsen family does care about the deep discount to NAV at which its shares trade in the market. Last year, they merged their two holding companies, Bonheur and Ganger Rolf, which jointly owned shares in the underlying businesses and had cross-holdings in one another. This made it easier to understand and estimate the value of Bonheur. This is still not an easy feat and there is still only one analyst on the sell side that covers Bonheur.

Italy has been a very rewarding market for us. Our large gains over the years in Italy were generated by investing in family-controlled holding companies trading at deep discounts to NAV. We have an investment currently worth $6.8 million in Cofide, the de Benedetti family holding company, which currently trades at a 42% discount to NAV. In a sense, Cofide is even cheaper than it looks because 22% of its NAV is net cash, some of which is being used to repurchase shares in the market, and a further 7% is investments in private equity and hedge funds. In March and April last year, we sold $3 million worth of shares in Cofide when its share price discount to NAV narrowed to less than 30%.

We have an investment currently worth $4.2 million in ASTM, the Gavio family holding company, which currently trades at an 20% discount to NAV. It owns high quality toll road assets in Italy. We took advantage of a 174% return on ASTM in Dollars last year and sold over $11.5 million in shares in the latter part of this year. Our investment in ASTM illustrates a very important point. When we make an investment, which we view in some respects as to being akin to planting a tree, we have no idea when it will blossom or fruit. We do expect it to happen within five years, but we cannot predict when it will happen, and indeed, it may never happen. In the case of ASTM, we purchased shares in the company because they were trading at a more than 50% discount to NAV. By comparison, most closed-end funds investing in infrastructure assets were trading at small premiums to NAV. We bought most of our holding in 2013 at around €9/share. We increased our shareholding by about 50% the following year at an average price of €10/share and bought a few more in 2015. The share price at the end of 2016 was €10.35, and by the end of 2017 it was €24.35.

We also have an investment in Danieli savings shares worth $6.7 million, a mini-mill maker and specialty steel manufacturer based in eastern Italy that is controlled by the Benedetti family (no relation to the de Benedetti's) who own 67% of the ordinary voting shares. This is a cash-rich business that has historically generated very high returns for its shareholders. Over the past 20 years, shareholders generated a return of 11% per annum. The shares look deeply undervalued at 12 times' currently depressed earnings, and even less on an ex-cash basis. In July, Camilla visited Danieli, ASTM and Cofide to get updates and to better understand their businesses. Mills is fluent in Italian, which is an asset when conducting business in Italy.

At the start of the year, we initiated an investment in Pargesa, controlled by the Frere and Desmarais families, which is now worth $6.5 million. We owned Pargesa a long time ago, but it came back on our radar after its share price nearly halved in Dollars from its peak in 2008. We bought the shares at a 40% discount to NAV in January. The share price has so far appreciated by 30% from our purchase price, but the shares still look very undervalued on a 35% discount to NAV.

Socfin, Sofinasia and Socfinaf are the Indonesian and West African palm oil and rubber plantation businesses that are controlled by the Fabri and Bollore families. Our investments in these three companies, which we have held for a long time, are worth $6.5 million. They remain deeply undervalued compared to their peers listed in Indonesia, Malaysia and Singapore, and even relative to peers listed on West African exchanges. This is due to their obscurity, being listed in Luxembourg. No brokers follow the companies and their free

floats are quite small. Over the past 20 years, shareholders in these three companies have compounded their investment at around 10% per annum, more than double the return of the MSCI Europe (US$) index.

Sonae is the Azevedo family holding company listed in Portugal. It owns the family's supermarket and retail businesses as well as shares in a property investment joint venture with the Grosvenor Estate in Portugal and a stake in NOS, the Portuguese TV, cable and satellite broadcasting businesses. The shares are trading at a 36% discount to NAV and we have a $5.4 million investment in the company. Portugal seems to be on the mend and we think this is one of the best ways to invest in a recovery of the country.

The Fund has an investment currently worth $8.6 million in Hansa Trust and an additional investment of $1.2 million in its subsidiary, Ocean Wilsons. During the year, we added to the Fund's holding in Hansa Trust as it trades at an anomalous discount to NAV. It is an investment vehicle set up by the Salomon family. Its closest counterparts are RIT Capital, an investment vehicle set up by Lord Jacob Rothschild, and Caledonia Investments which is an investment vehicle set up by the Cayzer family. All three families remain major shareholders in these London-listed companies. We have owned shares in Caledonia in the past. Currently, Hansa Trust "A" shares trade at a 29% discount to NAV. Prior to the financial crisis, it often traded at a small premium to NAV. This compares to Caledonia which is trading at a 15% discount to NAV and RIT which trades at a 9% premium to NAV. This disparity in valuations is unwarranted in our view. RIT Capital and Hansa have comparable track records of compounding NAV growth. Mills looked back at Hansa's track record and found that since 1995, its NAV increased by 9.5% per annum compared to 9.9% per annum for RIT. By comparison, the FTSE All-Share index compounded at 4.4% per annum over the period. Since September 2003, which is as far back as our NAV data for Caledonia dates, Caledonia compounded its NAV per share at 8.3%. By comparison, Hansa compounded at 9.8% per annum, RIT at 9.7% per annum, and the FTSE All-Share at 5.1% per annum over the same period. Bear in mind that Hansa also pays about a 2% dividend yield.

The attraction of Hansa is further magnified as it offers multiple levels of discount. In addition to the Hansa Trust discount to NAV, its largest investment is Ocean Wilsons, which makes up 31% of its NAV. Ocean Wilsons trades at a 26% discount to its NAV. Wilson Sons, which makes up 68% of Ocean Wilsons NAV is one of the largest operators of container terminals, oil and gas terminals, towage, shipyards, logistics and shipping agencies in Brazil. It has performed resiliently throughout the economic crisis in Brazil. Based on the price recently paid for the acquisition by an investor for a comparable container terminal in Brazil, this suggests that Wilson Sons trades at a 34% discount to the sum-of-its-parts. The reason why Hansa Trust trades on a wider discount to NAV than its peer group is because of its high exposure to Brazil, but we view that as a cyclical phenomenon and think that the quality of the Brazilian business is not appreciated.

Mytilineos is a new holding in the Fund, currently worth $5.8 million. We owned shares in Metka whose main business is the construction of large power generation plants, most notably highly efficient combined cycle power plants which it builds in emerging markets. Mytilineos made an offer to buy the 50% of Metka that it did not already own at a price that we felt inadequately reflected the fair value of Metka. We, and a number of other minority shareholders, opposed the deal, but we decided to retain the shares in Mytilineos as our interests are now more closely aligned with the interests of the Mytilineos family. Mytilineos is a low cost producer of electricity in Greece and is one of the lowest cost smelters of alumina and aluminum globally. Its track record is excellent. During the past 15 years, the Greek equity market declined by 75%, but Mytilineos compounded shareholders' money at 20% per annum. In spite of this track record and a positive outlook, the shares trade on a P/E of 7.6 times estimated 2018 earnings and a 3% dividend yield.

Neurones is a French IT services business in which we own shares currently worth $6 million. About 70% of its revenues are recurring from existing customers. Neurones is a capital light business that generates ample free cash flow, some of which they have historically used to invest in buying other similar IT services businesses. Luc de Chammard, the founder and CEO, is fanatical about his business. He is also good at allocating capital. Chammard and senior management hold over 75% of Neurones shares. Neurones focuses on addressing the specific needs of its Parisian customers and this specialisation enables it to charge premium prices. Over the past 15 years, Neurones has compounded shareholders' money at 16% per annum. Net cash accounts for about 20% of Neurones' market capitalisation. On an ex-cash basis, Neurones trades at 19 times estimated 2018 earnings. It is more fully valued than most of our other holdings, but it is a very well-managed company that is still relatively small with ample scope for future growth.

Other large holdings

As already noted, the Fund has an investment in Sberbank currently worth $11.9 million. We also have investments in Gazprom Neft worth $6 million and in Raven Russia worth $5.2 million. In total, we have 8% of the Fund's assets invested in Russia. Gazprom Neft is is the fourth largest oil producer in Russia, producing more than 10% of Russia's total oil production, and is the third largest oil refiner in Russia with a more than 15% domestic market share of refining throughput and service stations. It is a subsidiary of Gazprom, which owns about 96% of its shares. Its shares trade a P/E of less than 5, compared to more than 15 for Shell and over 20 for Exxon. Currently, it pays a dividend yield of about 4%, but the dividend could increase a lot given that the Ministry of Finance in Russia is pushing for state-controlled companies to have dividend payout ratios of 50% in the next few years.

Most of our holding in Raven Russia is through a straight preferred share, that at the current price yields over 8% in Sterling with no withholding tax, and a convertible preferred which yields 6.5% with an equity kicker at the current price. The shares yield an estimated 6% at the current share price and are arguably the most attractive part of the capital structure. Raven Russia owns a portfolio of modern logistics warehouses, primarily adjacent to the ring road around Moscow, but also on the outskirts of St. Petersburg. Their warehouses are valued at a cap rate of more than 12% so from a valuation point of view, it looks like a very attractive investment. We however feel more comfortable higher up the capital structure as we think that management is too lavishly compensated and made representations to that effect to the founding Bilton family.

The Fund owns 14% of Baker Steel Resources Trust (BSRT), making us the largest shareholder. Our stake is currently worth $10.2 million. The manager, Baker Steel, is a specialist natural resources investor, founded in 2001 by the principals David Baker and Trevor Steel who were founding members of the Blackrock mining team in 1992. BSRT's share shares trade at a small discount to NAV. Polar Acquisition Ltd (PAL) accounts for 37% of BSRT's NAV. PAL in turn owns 90% of Polar Silver, with the other 10% owned by Polymetal who are funding the feasibility study at the Prognoz silver mine. Polymetal is listed in London and has a market capitalisation of nearly £4 billion. Polar Silver owns 50% of Prognoz, and Polymetal thinks this is likely to be one of the largest and lowest cost silver mines in the world. Polymetal has an option until March 2019 to buy BSRT's PAL shares at a price based on the proven reserves and silver price at the time. Based on the estimated reserves and current silver price, it is reasonable to expect BSRT to record a large uplift in the current carrying value of its PAL stake when Polymetal exercises their option. This would have a massive impact on BSRT's NAV/share.

BSRT's next largest investments are Bilboes (13% of NAV) which is a gold mine in Zimbabwe producing small amounts of gold but which is doing a pre-feasibility study to increase production to 200,000 ozs/annum through open-pit extraction, and Ivanhoe (11% of NAV) which owns Kamoa, the world's largest, undeveloped, high grade copper reserves in the world as well as another high grade reserve in Democratic Republic of Congo, plus the Kapushi zinc reserves and Platreef platinum reserve in South Africa. Ivanhoe is backed by the billionaire serial mine developer, Robert Friedland, and the shares are listed in Canada. BSRT has been selling shares in Ivanhoe at incrementally higher prices. The shares are liquid and have appreciated by more than 500% in the past two years, but the manager thinks there is still quite considerable upside. There are a number of other holdings in the portfolio with exciting potential. This is our precious metals hedge in the Fund.

Gaztransport et Technigaz (GTT) has appreciated by 81% since we bought it in the summer of 2016 and is now worth $6.3 million. GTT is a leading provider of containment systems technology for the shipping and storage in cryogenic conditions of LNG (liquefied natural gas). I wrote about it extensively in last year's Chairman's statement. Two important things happened last year at GTT. They have been working on a new possible application using LNG as a propulsion fuel. In November, GTT won a major contract for the design of LNG fuel tanks for nine giant container ships ordered by CMA CGM, and in December, they signed a cooperation agreement with Wartsila to develop LNG fuel solutions. The other significant development alluded to in my earlier discussion of Altamir is the reduction in the French withholding tax rate. GTT generates prodigious free cash flow and has a cash-rich balance sheet so it pays a generous dividend. Based on the expected annual dividend, the shares yield 5.2% so the reduction in withholding taxes is very positive for non-French shareholders.

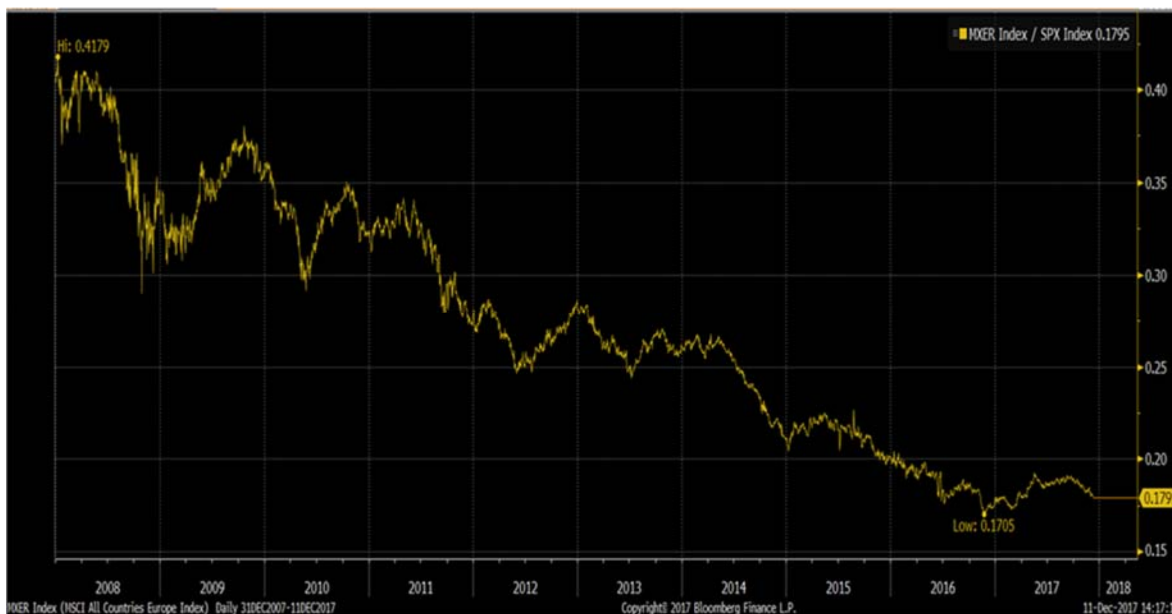
The Fund has had a longstanding investment in Yara International which the Fund has owned since it was spun off by Norsk Hydro in 2004. Yara remains the Fund's largest holding with a market value of $15.7 million. We sold a few shares during the year when its shares appreciated and it became a larger proportion of the Fund. It remains an excellent business which has provided its shareholders with a compound annual return in US Dollars of 19% per annum since we bought shares when it was listed in 2004. I said in last year's Chairman's statement that Yara should earn around US$2.50/share at the bottom of the urea cycle and around US$6.50/share at the top of the cycle, with the bottom and top of this range increasing over time. In 2017, which we think is likely to be the bottom of this cycle, Yara will likely only earn about $2.00/share. However, I said last year that growth initiatives already in place should add around NOK US$0.75/share to earnings by 2019. During the past year, Yara said that it has identified cost savings and growth initiatives that should add $2.00 per share to earnings by 2020. We therefore maintain our view that Yara's shares are undervalued at the current share price, equivalent to around $46; that its quality is higher than is widely appreciated; that it is less cyclical than perceived, and becoming less so; and that it earnings are likely to be significantly higher five or ten years from now.

<u>Stable assets and a portfolio that ought to produce decent returns</u>

The Fund ended the year with net assets of $282 million. Last year, the Fund had $3.3 million in subscriptions and $21 million in redemptions. Redemptions exceeded subscriptions for a few reasons. During the year, there were typical partial redemptions by clients to fund living expenses, plus a few by clients to help children buy their first property. We experienced one large redemption of over $6 million from a client who recently moved to England, whose tax considerations changed as a result, and another of only $1 million from the estate of a longstanding client who passed away. During the year, there were also multiple redemptions totaling nearly $5 million from our two Cayman pension plans who were required to sell part of their shareholding in the Fund as it appreciated, in order to remain within the parameters set by the Cayman

Islands National Pension (Investment) Regulations. We have also not done any marketing, continuing to rely on word of mouth referral from existing clients. We devoted last year's annual client seminar in March to explaining why we felt bullish about the Fund's prospects. That view proved prophetic.

The Fund ended the year with net cash of $40 million, well up on last year, as we struggled during the year to find attractive new investment opportunities at compelling valuations, though we added to some of our existing holdings opportunistically and purchased Pargesa at the start of the year and Better Capital 2012 throughout the year. The global stock market cycle is well advanced. However, this bull market has been focused on the US and the technology sector globally. European equities lagged US equity returns by a huge margin over the past 10 years as shown in the chart below, and last year was only the beginning of a rebound in the performance of European equities relative to US equities which we think has a long way to go.



The OAM team

Rob left us at the end of May. We will miss him and wish him well in this next chapter of his professional life. Rob was excellent at understanding and explaining complex accounting issues, and at untangling and making sense of consolidated and parent company accounts at holding companies. He was a master of spreadsheets. If Microsoft needs to know anything about Excel, they should call Rob. Sadly, Sheila is retiring this month after a more than 20 year career with OAM. She will be missed as an important member of the OAM team. After Hurricane Ivan in 2004, Sheila was invaluable to me so that I was able to keep up with my workload of running OAM and repairing the damage to our house at the same time. Sheila had damage to her own house to repair, so thank you Sheila for all your support and hard work, and for being a valuable sounding board over the years. In October, Naomi joined us from MUFG. Naomi is a CPA with more than nine years' experience in the fund accounting industry and has taken on responsibilities for fund administration. She is also assisting Sue with compliance which has become increasingly burdensome.

Camilla continues to co-manage the Fund with me, and is gradually increasing her primary responsibility for a greater proportion of the Fund's holdings. I continue to give guidance to Mills, suggesting possible new investment ideas to explore, and I read all internal research reports and monitor the Fund's holdings closely. It is helpful that we narrowed the Fund's focus during the past few years, so the task of following our holdings is now more manageable.

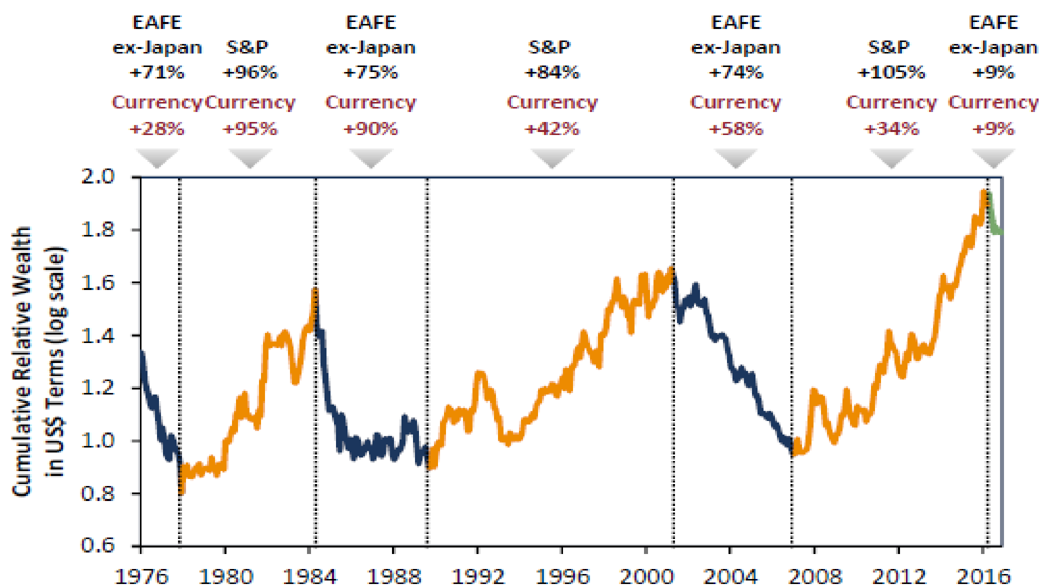
Outlook

We are very concerned at the increasing risk of a US stock market crash. US equities are more expensive than they have been at any time in the past 125 years on several measures, only surpassed in the months leading up to the 1929 Stock Market Crash and the Great Depression which followed, and the period surrounding the Dot Com boom and bust in the late '90's and start of this century. Neither were good times to buy US equities. If the US stock market crashes, everything else is likely to go with it. As my mentor, Paul Fenton, used to remind me: "On Wall Street, when the paddy wagon pulls up, they take the good girls along with the bad". If that happens, I expect a strong recovery in European equities after a large initial fall. At current levels, we think they are priced to deliver high single digit returns over the next ten years. This remains an attractive investment proposition in today's low interest rate world.

Every year, I read tens of thousands of pages of investment research and annual reports. This past year's prize for what I think was the best article on asset allocation goes to Jeremy Grantham who wrote an article in the second half of the most recent GMO quarterly newsletter entitled: "Career Risk and Stalin's Pension Fund: Investing in a World of Overpriced Assets" (https://www.gmo.com/docs/default-source/research-and-commentary/strategies/gmo-quarterly-letters/what-happened-to-inflation-.pdf?sfvrsn=5). Jeremy Grantham is one of my heroes in the investment business. There were two very useful charts in the report. One showed that the cyclically adjusted P/E (CAPE) of equities in the developed world ex the US is currently in the 'teens. The CAPE of US equities is currently 33. In the past, the CAPE for US and the developed world ex the US were broadly similar, but they diverged markedly during the past five years.

The other chart, on the following page, shows relative moves over more than 40 years between the US equity market as measured by the S&P 500 index and non-US equities as expressed by the MSCI EAFE ex-Japan measured in US Dollars. The reason for excluding Japan is that Japan had a massive equity bubble ending in 1990 that distorts the performance of the MSCI EAFE index over the period. EAFE stands for Europe, Australasia and Far East, so when we exclude Japan from EAFE, the remaining country constituents outside Europe account for around 15% of the EAFE ex-Japan index, making this a rough proxy for European equities.

Exhibit 4: US vs. EAFE ex-Japan



As of 9/30/17
Source: GMO, Standard & Poor's, MSCI

The chart on the previous page illustrates the periods in dark blue when EAFE ex-Japan outperformed the S&P 500 by 70-75% during each upward move, and the periods in yellow when the S&P 500 outperformed the EAFE ex-Japan. Interestingly, the 2007-2016 period was the largest margin of outperformance by US equities, so there is a reasonable expectation that European equities could outperform during the coming period by a very wide margin. The other interesting observation is that in every cycle, the currency has moved in the same direction as equity markets relative performance. This is probably a function of momentum in capital flows moving currencies as investors said during the post-GFC period that they loved the US but hated Europe. There is yet one more interesting point that emanates from the Grantham article. That is the attractiveness of emerging markets in today's world of low returns. Keen observers will note that we have a lot of exposure to emerging markets in the Fund. That is a deliberate policy on our part.

The Grantham article reinforces my view that even if US equities crash, the 7-10 year returns for our Fund's investors should be good, even at today's price levels. There is no doubt that a Wall Street crash would cause short-term pain globally, but at least the investment arithmetic makes sense today for our Fund's holdings. From my personal point of view, in spite of last year's strong run, I am unable to find another financial asset other than emerging market equities with a comparably favorable outlook, so I continue to maintain my family's large shareholding in the Fund which totals about 10% of the Fund's outstanding shares.

Desmond Kinch, CFA
Chairman