Memorandum

To : Forum Staff

From : BW

Date : April 19th, 2017

Subject : FES Chief Investment Officer Report on Q I 2017 Results

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This report of the CIO has been put together for **stakeholders interested in what FORUM Family Office ("FFO") does in the area of publicly-quoted companies**, mainly

a) our **internal professional** team as feedback how well we worked as a team – long-term investment performance is our ultimate scorecard

b) the **companies and their Executives** which share their time with us answering our questions to give them a better understanding what type of investors they are dealing with

c) the close to 1.000 p.a. **applicants to FORUM** to help them understand what they should expect when joining FORUM.

At times we will refer to our activities in the publicly-quoted space as **FORUM European Smallcaps ("FES").**

This Report covers the **Q I 2017** period**.**

For a deeper understanding of what we do and how we think we would like you to look at the three Appendices at the end of this Letter:

a) Appendix 1: Methodology for calculating our results in publicly-quoted equities

b) Appendix 2: Summary of our Investment Philosophy

c) Appendix 3: Glossary

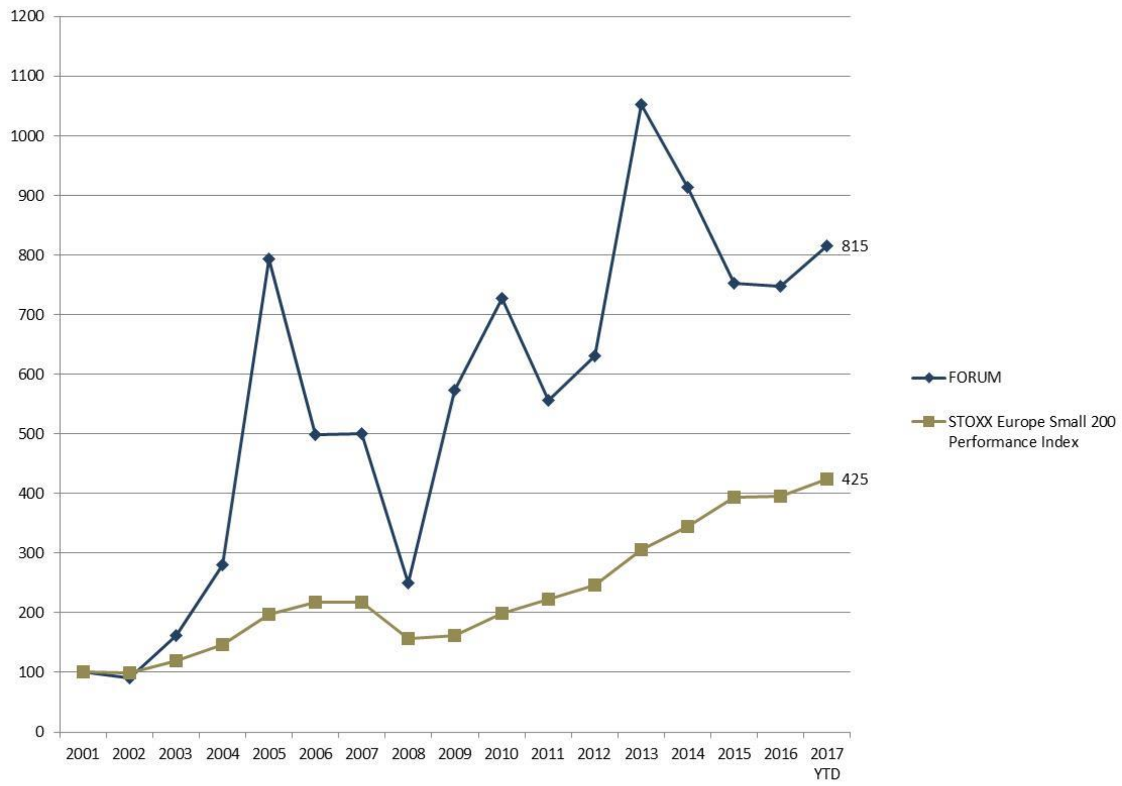
1. Results in Q I 2017

1.1 Benchmarking of Results at Market Prices

For an overview of **our results vs. our benchmark** please refer to **Chart 1 below**.

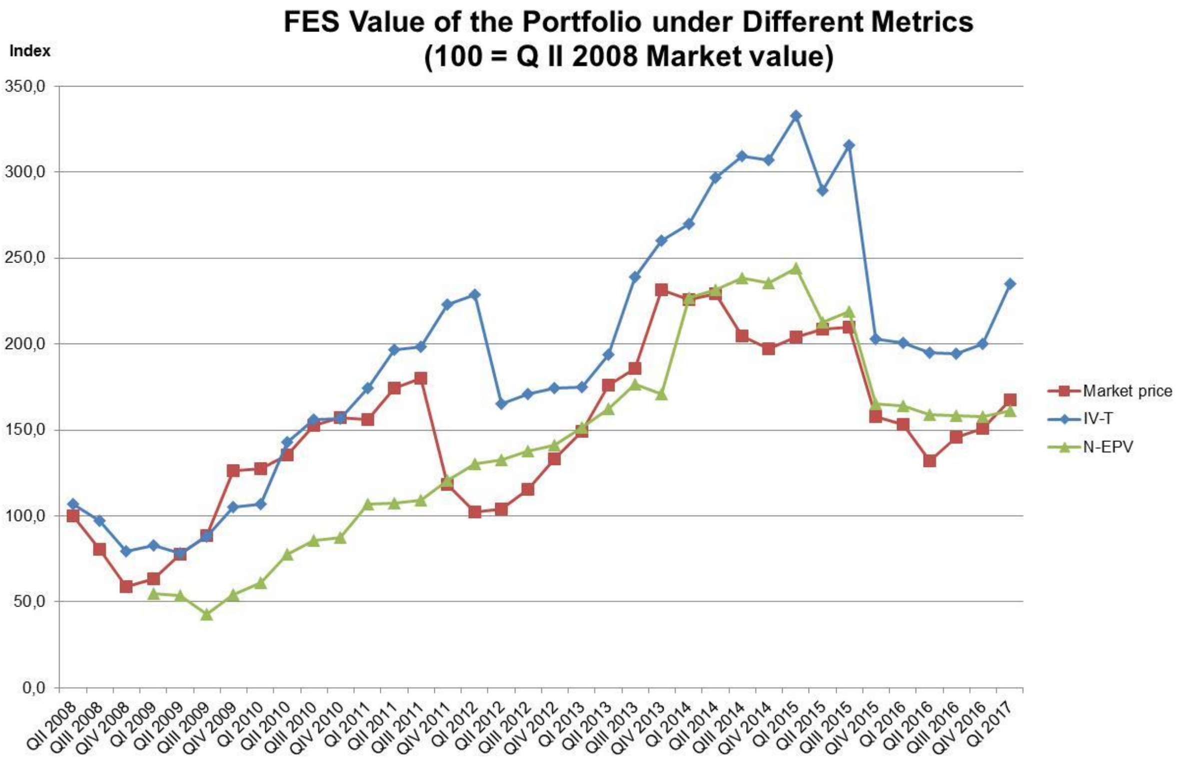
In Q I 2017, **our performance was 9,1%**, vs. the STOXX Europe Small 200 index increasing by 7,4%. This is an **outperformance of 1,6%.**

This brings the **IRR of the fund since inception to 14,8%** p.a. - compared with the benchmark index generating an IRR of 9,9% p.a.



1.2 Results at Market and Intrinsic Values

Please see the graph in **Chart 2 below** for an overview of the portfolio over time :



a) **The line in green shows the value of the portfolio at Net Earnings Power Value ("N-EPV").** N-EPV captures the Earnings Power Value of the existing business **in a steady-state situation – i.e. does not attribute any value to growth.** We calculate it by

- simulating how much cash the business could generate if there were no re-investments into growth and

- capitalizing this cash flow.

Thus this is a very conservative valuation – making no estimates about future growth which will always be uncertain.

In the quarter **N-EPV increased sequentially by 2,1%.**

The companies we added to our portfolio were trading close to N-EPV, explaining the small increase over the quarter.

b) The line in blue shows the value of the portfolio at IV-T – i.e. including the value of growth.

In the quarter **IV-T increased sequentially by 17,4%.**

The strong increase in the quarter is mainly due to the addition of new positions with what we consider a significant upside potential, mainly our two Mexican holdings and a European pharma company.

1.3 Margin of Safety

To interpret **Margin of Safety** of the fund, look at **Chart 2** above again. Now you should focus on **how the red line – depicting NAV – is moving relative to N-EPV and IV-T.**

1.3.1 NAV vs. N-EPV

NAV reflects the prices paid by the market for our stocks. N-EPV is the value we assign to our holdings for the steady-state businesses.

As the stock market puts some value on growth, it is **normal that NAV is above N-EPV**. At the end of the last quarter **NAV was ca. 6% above N-EPV.**

Inverting this ratio, N-EPV is at ca. 94% of NAV. A simplified interpretation of this ratio would be to say that **ca. 94% of the NAV of the fund is covered by N-EPV - i.e. the capitalized cash flows of our businesses, modelling them as ex-growth businesses.**

This is **a good Margin of Safety,** in line with historical values.

1.3.2 NAV vs. IV-T

IV-T measures the value of the businesses we own including the value of growth. We would like to see NAV below this value, as the difference between the 2 metrics gives an indication of the upside which is not (yet) priced into the share prices.

At the end of Q I 2017 **IV-T was 47% above NAV.**

Remember that **IV-T is calculated by discounting the future expected value of the business back to today.** Our discount rates are in the 8 – 12% p.a. range. Thus if the market price of a share reaches IV-T you can expect an IRR of 8 -12% p.a. by holding this position.

If in addition IV-T is above NAV- which is the situation today - there is potential for additional returns from higher valuations. Thus we feel comfortable with this metric for protection/upside as well.

1.3.3 Summary of Margin of Safety

With:

a) 94% of NAV underpinned by N-EPV, giving good downside protection

b) IV-T ca. 47% above NAV, signaling that the market prices have room to increase before they reflect the full value of what we own

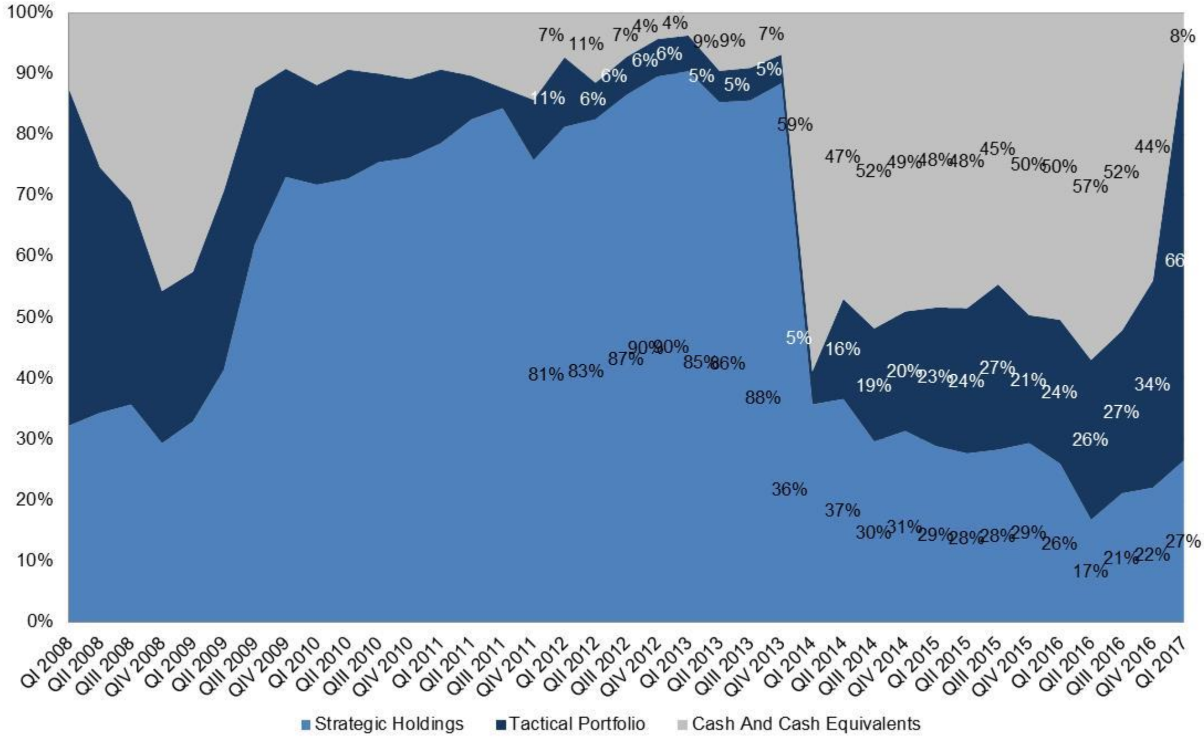
the Margin of Safety of the portfolio **has swung from being slightly below the historical average observed at FORUM Family Office to being higher than average**.

This makes us mildly optimistic for the remainder of 2017.

2. Asset Mix and Results by Asset Class

2.1 Evolution of Asset Mix

Please see **Chart 3 below** for an overview of the composition of our long book.



As you can see in Q1 2017 we invested a significant portion of our cash into tactical positions. At the end of Q1 2017, the portfolio mix is:

	% Portfolio
a) Strategic	27%
b) Tactical	66%
c) Cash and Equivalents	8%
d) **Total**	**100%**

Net long exposure is 90,7% (92,4% long ./. 1,7% short).

3. Strategic Holdings (27% of NAV)

3.1 Immunodiagnostic Systems Holdings ("IDS")

In Q1 2017 the key change at IDS was the announcement that Patricio LACALLE, which had been CEO since April 2015, was being replaced by Régis DUVAL.

After successfully converting Pulsion into a wonderful investment case and implementing the roots of a successful restructuring at IDS, Patricio has decided to pursue other personal opportunities. **We thank him for his dedication over the last 6 years and wish him all the best for the future.**

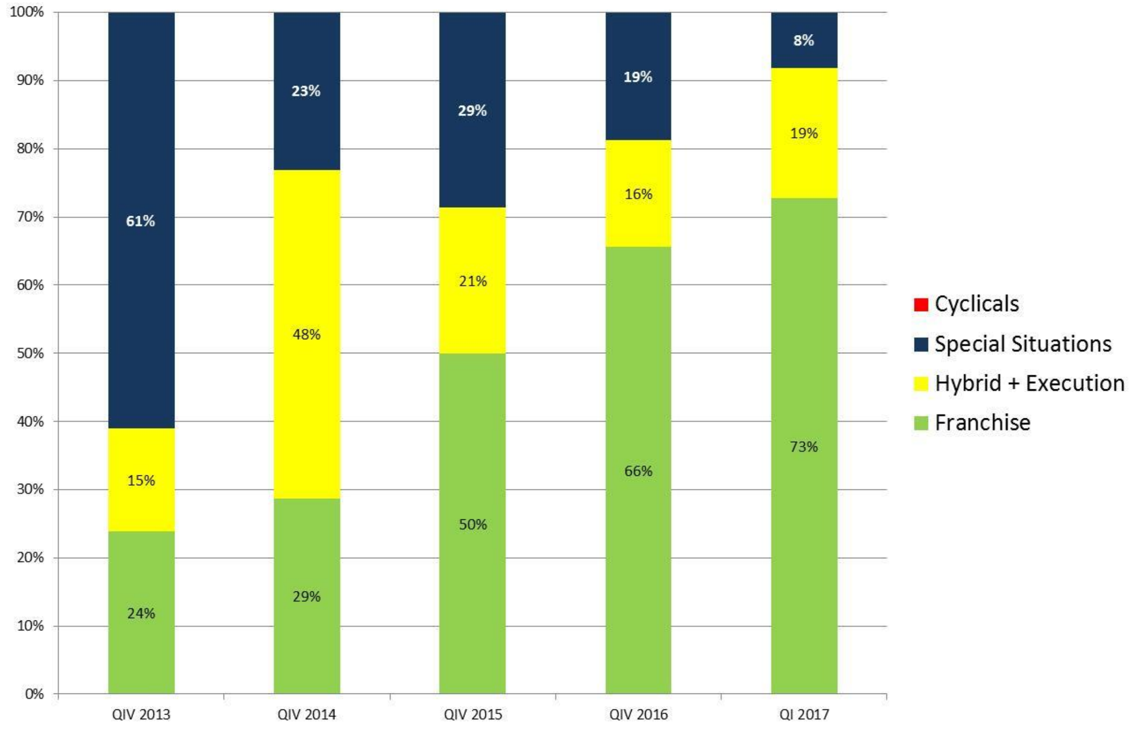
Régis was most recently head of Sales Europe at Bio-Rad, where he stayed the last 6 years in various positions. We hope that he will be able to lead IDS back to growth.

3.2 New Candidates

We did not add any new investments to our strategic portfolio in Q I 2017.

4. Tactical Portfolio (66% of NAV)

The chart below gives an overview over the **types of investments** making up our tactical portfolio.



4.1 Franchise Businesses (48% of NAV)

These are **businesses of highest quality - combining high customer stickiness with a strong competitive advantage**. Historically they have been at the core of what FORUM does, mostly accounting for ½ - 2/3 of our assets. This class of businesses will stay at our core in the future as well.

With **48% of NAV** this class of businesses has reached an all-time high. This part of the portfolio has grown from three positions a year ago to **six companies**. Other than the attractive business characteristics most of these companies have CEOs which we would rate as outstanding (that is at least 57/60 on our scoring model).

During the quarter **we added one new Franchise Businesses** and increased our allocation to several others. In two cases the opportunity came from Donald Trump – one is in renewable energies and one in pharma, both of them European businesses with a significant US exposure.

As we are still building positions in this group we would prefer not to talk in more detail about these businesses.

4.2 Hybrid and Execution Businesses (19% of NAV)

These are the businesses of **medium and lower quality**. They have in common that they are largely in control of their own destiny – unlike the commodity/cyclicals businesses in the next category.

The industries in this group range from machine components to roadside assistance. In these businesses the quality of **management is immensely important and we spend a lot of time in our Due Diligence to verify it**.

The weight of this group has increased **from 5% of NAV at the end of 2016 to 13% at the end of Q I 2017,** largely due to 2 additions. At the end of Q I 2017 we had **5 companies in this group**.

At the same time we disposed of 2 businesses in this category because we saw risks – which would hurt businesses in this category more than e.g. the Franchise Businesses.

4.3 Special Situation (8% of Tactical Portfolio)

This category consists mainly of a Genuss-Schein of Commerzbank. The current yield to maturity in 2020 is 4,75% p.a.

According to Basle II it does not qualify as tier 2 equity; the percent counted as equity will decrease by 1/10 each year – making it increasingly unattractive to the bank. **Thus we expect an offer for early redemption.**

The other position is Stada – which we entered after discussing their plan with the two activist investors, as well as after doing our own Due Diligence. If we become activist ourselves we would group such a business in the “strategic” category.

4.4 Cyclicals

We add cyclicals to our portfolio as we believe they can add good returns if picked at "deep value" valuations - e.g. a mining supplier when a significant part of the commodity supply is losing money on a cash basis.

And we believe **we can build an edge combining our frameworks on long-term profitability with the psychological edge – vulgo guts** – required to buy when the institutional mainstream believes the world is going under.

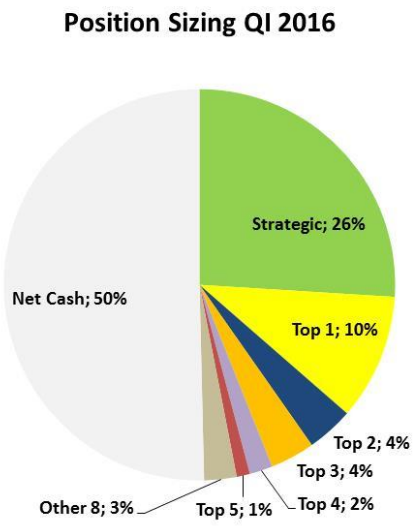
As you may remember we have had **M.P. Evans** in this category after the special situation worked out according to our thesis. When we were left with a pure commodity producer and the price of the commodity was near its long-term average we closed the position in Q I 2017. Over the 3 years holding period it generated a return of ca. 12,7% p.a. in LC.

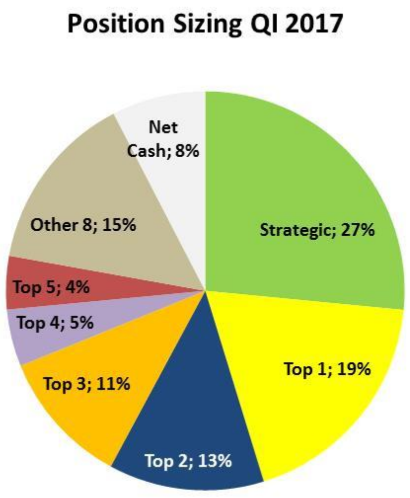
Thus at this stage we have **no cyclicals in our portfolio**. And as the key success factor is to buy when a cyclical is REALLY CHEAP, we have few ideas in the pipeline – nothing appears to be REALLY CHEAP these days.

5. Other Aspects of Portfolio Management

5.1 Portfolio Concentration

Please see below an analysis of our portfolio by size of holding.





We continue to have a rather concentrated approach:

a) Our strategic holding account for 27% of AUM

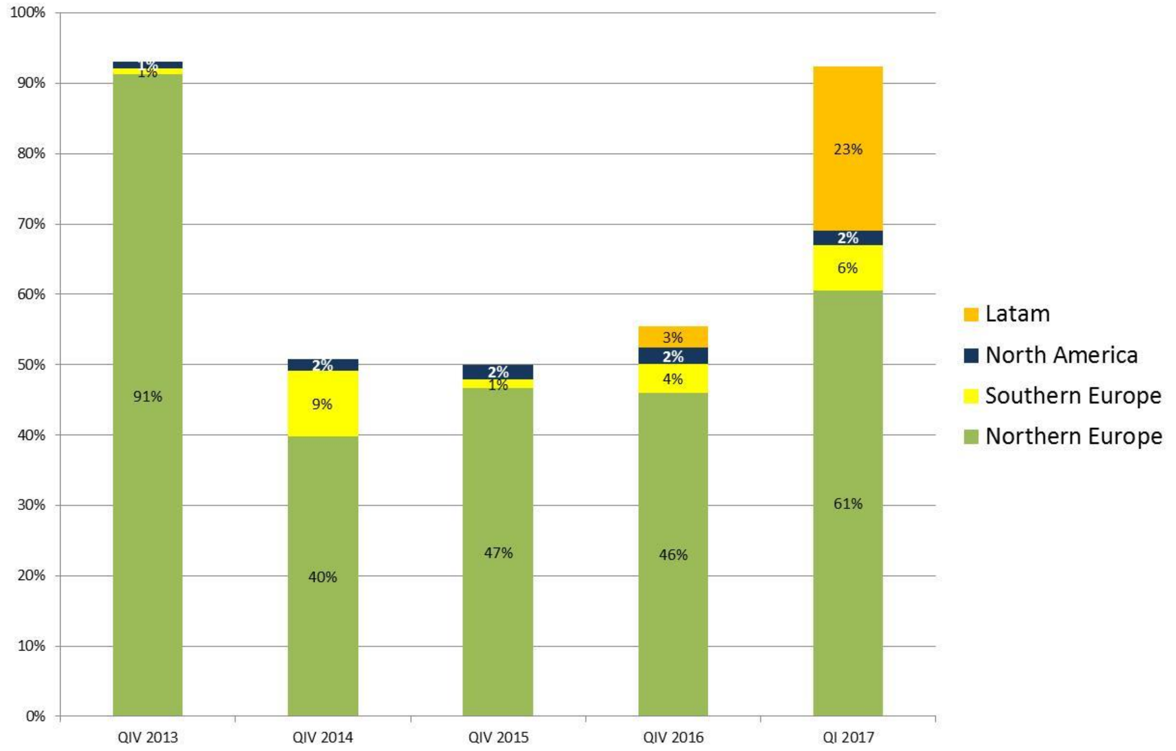
b) The **top 3 holdings of the tactical portfolio account for ca. 43% of net AUM**

Compared with a year ago we have built-up strong number 2 and 3 positions.

With respect to the "tail end", i.e. our smallest positions below the top 5 we have increased their weight to 15% of AUM, up from **3% a year ago. The number of positions is unchanged at eight, thus the average weight per position has reached ca. 2,0%.** Some of these are positions where we initiated a small stake and wait until we have finished our Business Due Diligence ("BDD"). We will strive to avoid carrying insignificant positions.

5.2 Portfolio Composition by Region

Please find below an overview of FES allocation by regional area (depending on Headquarter location):



As announced we have built up **positions in two companies headquartered in Mexico.** They have now reached a combined 23% of net AUM. We got into these positions after the Mexican Peso crashed following the election of Donald Trump (again two investment opportunities handed to us from the man), and since then it has recovered nicely. We continue to be in close contact with the company and its management.

In term of economic exposure of the 23% of net AUM ca. 14% are linked to Mexico itself, ca. 6% to various countries in Latin America and ca. 3% to the USA.

Secondly some of our investors have asked about our exposure to Northern vs. Southern Europe. As you see at this stage **our European exposure is largely concentrated on Northern Europe**. This is by opportunity rather than by design – we just have found the better companies in Northern Europe.

6. Short Book

At the end of Q I 2017 FES had 3 short positions. The combined weight of the short positions accounts for 1,7% of AUM, thus it is not significant. We intend to increase this weighting.

7. Risk Report

We would like to refer you to the extensive discussion of the major risks facing the firm in the Report of the CIO 2016. **Since then there have been no significant changes.**

8. Outlook

8.1 Macro Outlook

We refer to our **Macro Dashboard for Q I 2017**. Since our last Macro Dashboard:

a) little has happened **in Europe**: corporate profitability has stayed around its historical averages, valuations have gone up slightly.

b) the **valuation bubble in the USA** has further inflated: both Shiller´s CAPE and market capitalization as % of GDP is at or close to two standard deviations - reaching levels last seen in 1929 and 2008.

c) The level of valuation in the USA relative to Europe - based on CAPE - has also reached historical levels - from which it has historically retreated in the subsequent 5 - 10-year period.

Thus we feel with our focus on Europe we sit in the right region in the world to deliver reasonable investment results. But if the overvaluation in the USA starts to correct it will definitely also affect our European holdings - but in price, not in Intrinsic Value**.**

8.2 Portfolio Positioning

As a result of the balance between upside and risk we target the following allocation top-down**:**

a) **Net cash** (i.e. after offsetting gross cash in the accounts against our short exposure) should be ca. 20% (it was at 8% at the end of the last quarter).

b) We are targeting **a short exposure of 10 - 15%**. We will continue to restrict ourselves to "autonomous shorts" - i.e. investments with a clear company-specific catalyst. This makes it difficult to reach this allocation.

Thus net long exposure should decrease to 65 - 70% - below the 92% we had at the end of Q I 2017.

And as always we will be driven by opportunities - bottoms up - if an attractive investment opportunity emerges we will take it, explaining the discrepancy to date.

9. The Firm

At the end of Q I 2017 our investment team consists of

a) 4 associates with at least 2 years of seniority at FORUM or equivalent outsides

b) BW as portfolio manager.

We are trying to add another analyst or associate to our team - if you know any candidates or read this yourself - help us fill this position!

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Burkhard Wittek

Appendix 1: Methodology for Calculating FES Results

1. Segregation FES and FPE

FORUM Family Office ("FFO") has an Investment Philosophy to **only invest in companies.** We have no real estate, no hedge funds and own no shares in forests etc. We do this in **several sub-classes of assets:**

a) Publicly-Quoted: controlling Stakes/Strategic Positions with Board Involvement

b) Publicly-Quoted: tactical positions which are liquid

c) Private Equity.

To hedge our exposure to the cyclicality equity markets we also **have a book of short positions in publicly-quoted companies.**

To calculate the results of the publicly-quoted part of our portfolio – i.e. long and short positions – we use the following methodology:

a) We value our PE holding at Investment Cost, i.e. their value is constant over time

b) The change in market value between 2 periods is calculated as the difference between the full value of our wealth

c) The gain /loss in percentage is calculated as the ratio between the change in Market Value, divided by the Value of our portfolio excluding the PE portfolio at the beginning of the period.

Below is an example of the calculation (fictitious numbers):

	Year N	**Addition to PE** (at cost)	**Year N+1**
Cash	10	-10	0
Listed Portfolio	80		90
PE Portfolio	10	+10	20
Total Wealth	**100**		**110**

Performance of the Listed Portfolio + Cash:

$$\frac{Total\ Wealth\ (N+1) - Total\ Wealth\ (N)}{List\ Portfolio\ (N) + Cash(N)} = \frac{110-100}{80+10} = \frac{10}{90} = +11{,}1\%$$

Appendix 2: Summary of Forum Investment Philosophy

1. Long Book

Our Investment Philosophy has **the principles of Value Investing as interpreted by Warren** Buffett at its core: we invest with a Margin of Safety in businesses which we understand well.

We think about our ability to understand a business well - i.e. **our Circle of Competence** - as follows:

a) We have an "**outer Circle of Competence**" which defines the limits of what we do. Regionally this is Western Europe. In terms of type of businesses we have to be able to understand their products, business models and the "systems" of customers and competitors they are operating in. **We do not invest outside of this outer Circle of Competence.**

b) There is also an **"Inner Circle of Competence**" - companies which we understand particularly well. These are companies which have a more or less simple product or service offering, we have been following their industries for many years or even decades and we can assess the CEOs. **This is our "sweet spot",** here our confidence in any valuation and risk assessment is the highest. This sweet spot should constitute the majority of what we do.

c) We will be willing to pay more for companies in the sweet spot than for companies within the outer Circle of Competence, but outside this sweet spot.

In terms of company size **we focus on small- and mid-cap companies** – which we define as companies with market capitalizations in the € 300m to € 2bn range.

When we make an investment decisions we start by looking at "**What we Get**": to us the most important aspects are:

a) **Business Quality:** the category we like most are **Franchise Businesses** with a strong customer franchise and a strong competitive advantage. Second in rank come **Hybrid Businesses**. And the businesses requiring the biggest management attention and having the lowest visibility are **Execution Businesses.**

We try to have a significant part of our assets in Franchise Businesses. At the same time this is not a dogma: there are periods where these businesses are grossly overvalued by the market, allowing no attractive returns - just peace of mind. E.g. the so-called "**Nifty-Fifty**" favored in the 1960 had a great run until 1972, then the bubble burst. In the subsequent 7-year period this group of highest-quality stocks underperformed the S&P 500 by 30%.

We do not go for "peace of mind" - but for risk-adjusted returns. At this point in time it is increasingly difficult to find such businesses at valuations allowing our target returns. In this interest rate environment such businesses are priced like "bond-substitutes".

b) **Management and Governance:** in any business the CEO, the rest of the management team and the Non-Executives on the Board can make a huge difference to what shareholders will earn over time. A business with 15% ROE **will double the equity base it has built up in its lifetime in the next 5 years**: how this money is spent/re-invested can create of destroy a lot of value.

c) **Internal Compounding,** i.e. the ability **to grow profitably**: in the long-run a business which has the option to grow at high rates while requiring little capital will generate enormous value from compounding - and current valuations do often not reflect the difference in sustainable growth rates between businesses.

   Therefore we look for **visible growth with a long runway**. With real GDP growth in Europe at 1 -2% at best this is not an easy task. Companies able to pick up bolt-on acquisitions at value-creating multiples and the ability to do Post-Merger integration have created such a system, **sometimes referred to as roll-ups**. We have several of them in our portfolio.

Based on the results of "what we get" we will then decide "**what we pay**". The principles are:

a) At the core of our valuation is the **Net Earnings Power Value ("N-EPV")**. We define N-EPV as the capitalized value of the cash flows the business can achieve on a sustainable basis assuming no growth. This value anchors us on paying only for "what is there today".

b) Even for the best businesses - Franchise Businesses, high management quality and visible profitable growth - we will not pay substantially above N-EPV. This is our definition of the **Margin of Safety.**

c) In any case we **require an expected return of 20% p.a.**

We define **risk as the permanent loss of capital.** If the risk of permanent loss of capital is more than insignificant we will not invest - even if the upside appears promising.

Conversely**, share price volatility is not important to us** - we consider these fluctuations mostly statistical noise. Instead we review the underlying earnings power of the businesses regularly: is it unchanged or has it been impaired?

We are looking for investors who share this definition of risk - they will have a long-term perspective on investing like we do.

2. Short Book

Our **short investments** serve three purposes:

a) Autonomous opportunities from overvaluations with a catalyst

b) Hedging of company-specific risks in long positions

c) Hedging of the overall portfolio against market overvaluation.

Within the short investments we have

a) conviction bets

b) stochastic bets.

As in shorting the long-term trend is against us and there are non-calculable event risks, e.g. a takeover - we have so far only had one conviction bet - **otherwise we do stochastic bets, spreading event-risk over many positions which will work out "on average".**

Appendix 3: Glossary

Execution Business: a business which needs the right management decisions every day to perform well. Conversely, it has little customer stickiness and low competitive advantage.

Franchise Business: a business with high customer stickiness and a strong competitive advantage. Companies in this group would be strong brands in FMCG, software companies with critical applications and a revenue model based on recurring revenues or companies with network economics

Hybrid Business: a business which has characteristics both of Franchise and Execution Business

Net Asset Value ("NAV"): the value of the fund at market prices.

Net Earnings Power Value (“N-EPV”): it captures the Earnings Power Value of the existing business in a steady-state situation. It is calculated based on after-tax cash flow to enterprise value (i.e. before interest rate) after eliminating expenses/cash out for growth. We also base it on a level of earnings considered mid-cycle earnings, i.e. we adjust actual earnings we consider them peak or trough earnings.

We then capitalize this cash flow metric – we refer to it as “**Owner Earnings**” or “OE” – with a cap factor based on business quality and market capitalization. E.g. for a large-cap franchise business we capitalize Owner Earnings with a factor of 12x.

Total Intrinsic Value (“IV-T”): it captures the total value of the business which is the sum of its N-EPV, structural improvements of the business and the value of expected growth. As such it contains several critical assumptions about the future and is less reliable than N-EPV.

IV-T discounts the future expected value – thus if the market price of a share reaches IV-T you can expect an IRR of 8 -12% p.a. – this is the range of discount rates we use.