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January 17, 2019

To My Partners:

2018 Performance Summary

From January 22, 2018 (fund inception) to December 31, 2018, Pinchot Lane Partners LP ("PLP", the "Fund") returned -10.3%, net of 0.75% in management fees. Below is a summary of Fund performance to date. I've included a column for the performance of "ACP units," which show returns of my personal stake in the PLP portfolio since January 1st compared to the S&P 500 index. The purpose of this column is simply to demonstrate what Fund performance would have been had the Fund started on January 1st (a more useful comparison when evaluating against index benchmarks). Due to the steep increase in the fund's value during the first three weeks of January (before the fund opened to limited partners), there was a meaningful difference between performance as measured from January 1st vs. inception.

	Calendar Year-to-date thru 12/31/2018	Fund Inception* thru 12/31/2018
(1) Pinchot Lane Partners LP Units**	*N/A*	*-10.3%*
ACP partner units**	*-2.3%*	*-10.3%*
(2) Benchmark: S&P 500 incl dividends	*-4.4%*	*-9.1%*
Relative Performance (1) - (2)	***2.0%***	***-1.3%***

** Fund inception was 1/22/18*
*** Net of YTD fund management fees*

While the fund's calendar year performance was better than the index, it was a challenging year to unearth the types of value situations that underpin the investment philosophy of PLP. In retrospect, instead of investing capital in high quality companies at merely *reasonable* valuations, it would have been better to insist on high quality at *cheap* valuations. Hindsight is 20/20, but 2018 proved to be a year in which such patience and waiting for the "fat pitches" would have been rewarded.

While unsatisfied to report a loss in 2018, I remain focused on good process and the long-term prospects of the fund. In any given year, the fund's performance can vary widely given its concentration (as of 12/31/18, the top 5 positions in the fund represent 46% of the portfolio). Moreover, as discussed previously (Ground Rule #3), PLP is not a hedge fund. Our goal is to generate attractive long-term returns predominantly by buying and holding undervalued equities. Investors who find it difficult to control emotions and function normally when stocks decline 20-40% probably shouldn't be invested in the market.

The Investing Environment in 2018

> *After a time, you may find that having is not so pleasing a thing, after all, as wanting. It is not logical, but it is often true.*
> – Spock, Star Trek season 2, episode 1 (1968)

> *Be careful what you wish for, you might just get it.*
> – Unknown

2018 kicked off with a massive rally (S&P 500 +5.6% in the month of January 2018 alone), reflecting an ebullient business environment and extending strong gains from 2017, which saw +23% total returns in the S&P 500 with relatively low volatility. The trailing 12-month price-to-earnings (P/E) ratio at the end of 2017 was 20.3x (the highest year-end trailing P/E multiple over the last decade), partly explained by market expectations boosted by the Tax Cut and Jobs Act (TJCA), which slashed federal corporate tax rates from 35% to 21%. The TJCA had a huge effect on corporate earnings, as illustrated by the following example:

	Pre-TJCA	Post-TJCA
Pre-tax Earnings	100	100
Tax rate	*35%*	*21%*
Post-tax Earnings	**65**	**79**
% increase	→	*22%*

In 2018, for your average tax-paying, US-domiciled corporation, the substantial reduction in tax rates meant pre-tax earnings didn't need to grow a penny to generate 20%+ post-tax earnings growth. While the promise of the TJCA in elevating and sustaining GDP growth over the long term remains to be seen (a requirement for the TJCA to pay for itself rather than merely ballooning the federal budget deficit), in the short term it has been a godsend for corporate earnings growth.

So why did the S&P 500 index end 2018 *lower* (-6.2% to be precise) than the beginning of the year? It's always a difficult proposition to rationalize market movements considering the number of different factors involved; at its core, "the market" reflects the volatility inherent in human nature. More likely than not, expectations of robust earnings growth driven by the TJCA were already factored into elevated index levels at the end of 2017. When earnings growth played out as expected in 2018, perhaps investors moved on to new headlines (e.g. Chinese tariffs, political instability, federal reserve policy), stirring new fears and uncertainty.

As value-driven, long-term investors, we don't have to parse the fickle winds of short-term public sentiment too carefully. The job we have is simple, yet difficult to execute consistently – search for objective truth, maintain rationality, know what we don't know, and understand how to price assets (I know, it doesn't exactly roll off the tongue).

Comments on the Current Portfolio

Throughout 2018, there were several opportunities to realize profits in long-held positions, including one that was bought out at a substantial premium. At the end of the year, there were 15 names in the PLP portfolio, down from 20 at inception. Due to profitable disposals, partners will owe a small amount of taxes on realized gains (mostly long-term). Further commentary on tax preparation is included at the end of this letter. As a reminder, sell decisions in the portfolio are not driven primarily by taxes, though they are considered within the bigger picture of optimizing long-term, after-tax performance. Attached in Exhibit A are the fund's top 5 positions as of December 31st.

As a general philosophy, the fund does not churn positions rapidly, given the high bar required for a new name to enter the portfolio. Below is a brief overview of the core questions I use to approach potential new investments:

- Is this a situation that I understand and that lies within my "circle of competence"?
- Can I reasonably expect the asset to exist 5-10 years from now?
- How is this asset positioned competitively?
- What regulatory considerations affect the future and underlying economics of the asset?
- Does the asset depend on leverage (debt) to create adequate returns?
- How does the asset perform in a variety of economic environments?
- Is the asset attractively priced based on readily ascertainable data and a sufficient margin of safety?

Every good long-term investor tends to have a comprehensive checklist that is both general (like the above) and specific to a particular asset/company. From a standing start, a considerable amount of work is necessary before committing precious capital to a new name. Fortunately, knowledge about business tends to compound, shortening the time required to gain deeper fluency on a new idea.

For existing investments in the portfolio, this checklist exercise is ongoing. Good investors are constantly checking and re-checking their investment theses to decide whether to remain invested in a position and how to size it in the portfolio. Moreover, good investors aren't beholden to any favorite positions and know that everything in the portfolio is for sale at all times.

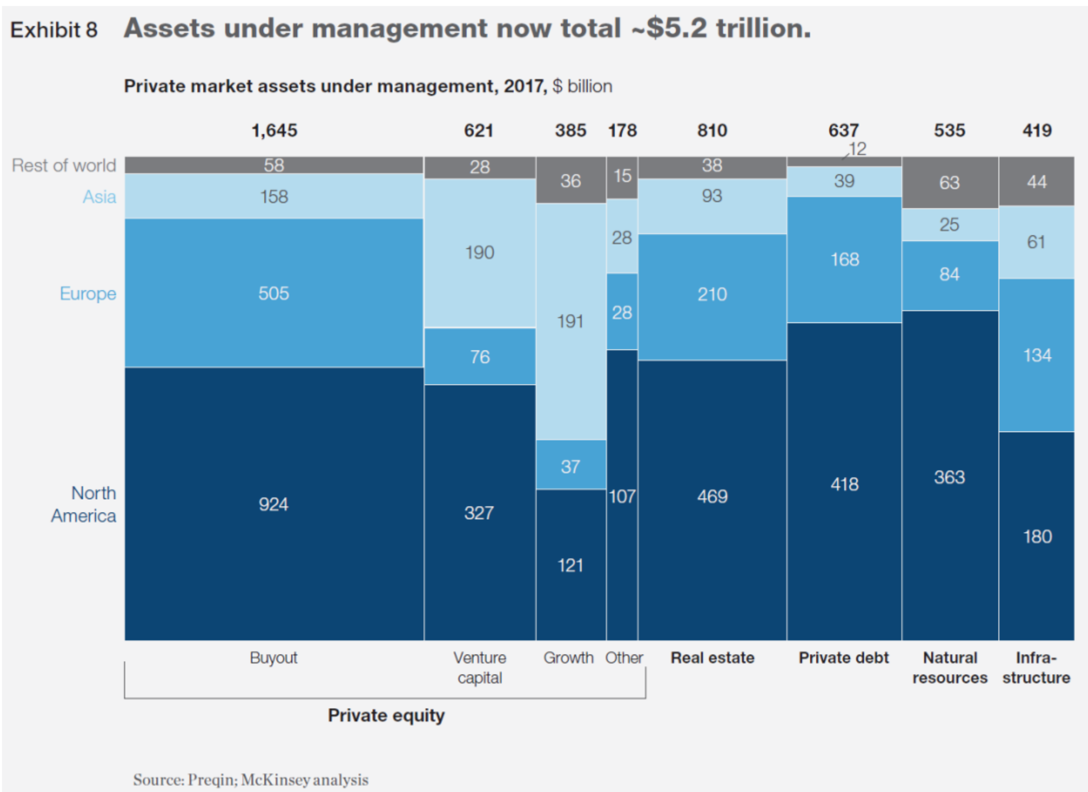
In the fourth quarter, the PLP portfolio turned over slightly more than usual in response to attractive new opportunities found in the market pullback. As situations with superior risk-adjusted returns arise due to new developments, I don't hesitate to rotate capital from existing positions into new ones.

If this approach to investing sounds straightforward, I assure you that it is not. Successfully managing investments can never be summarized in a “how to” manual.

> *It’s not supposed to be easy. Anyone who finds it easy is stupid.*
> – Charlie Munger

A Word on the Private Markets Phenomena

In the past decade, global private asset classes have exploded in size, growing to over \$5 trillion[1] in assets under management (AUM) compared to \$80 trillion in global AUM.[2] Private AUM has more than doubled over the last five years alone.



Institutional and high net worth investors have aggressively increased capital allocations to private markets on the belief that these assets offer superior returns with less risk.[3] First, a bit of background.

Private markets encompass an extremely broad set of investments in non-publicly traded assets, including operating companies, real estate, infrastructure, commodities, debt, startups, and derivatives. Almost anything that accepts money as a form of participation can be made “private.” Private assets generally don’t trade on an

[1] “The rise and rise of private equity,” McKinsey & Company, [February 2018]
[2] “Global Asset Management 2018: The Digital Metamorphosis,” BCG, [July 19, 2018]
[3] “Angst-ridden investors continue equities exodus,” Financial Times, [January 6, 2019]

exchange and are typically more illiquid. As a result, their prices are not necessarily transparent or obtained with ease. Furthermore, detailed information on private asset performance (e.g. sales, cash flow) is not widely disseminated, if at all.

In contrast, publicly-listed assets are generally “traded” on exchanges - prominent clearinghouses of buyers and sellers governed by regulations concerning the nature of trade and the routine disclosure of information. In these marketplaces, buyers and sellers declare the prices at which they are willing to conduct trade, and a historical record of transacted prices is made available in the public domain (there are a few exceptions to this transparency which we won’t detail here as they aren’t relevant for the current discussion).

While private assets and the funds that hold them are often marketed as unique or proprietary, it’s important to recognize that the entirety of the investable universe is comprised of assets; whether these assets are labeled public or private does not fundamentally change what they are. An asset is not made good or bad, or better or worse, just because it is private or public. It’s what managers and shareholders do with these assets that counts.

What might management teams do differently or better in private markets than public ones? From an investor standpoint, when is it better to own a private asset vs. a public stock?

Below is a list of arguments for and against private ownership from the perspectives of managers, employees, and investors:

	Edge			
Parameter	**Private**	**Public**	**Theory**	**Practice**
• Management strategy & execution	X		• Mgmt less pressured to make decisions based on short-term optics	• PE firms often invest on 3-year time horizon, constantly thinking about an exit
• Operating costs	Push		• Companies can avoid costs of public co. SOX compliance	• Far from being a public co. check-the-box exercise, SOX compliance benefits all companies

Parameter	Edge		Theory	Practice
	Private	Public		
• Access to financing	Push		• PE firms often make claims of tapping into credit markets on more beneficial terms, given “repeat customer” status	• Same competency can be shared regardless of ownership structure
• Asset valuation	Push		• PE firms once claimed less competition in private markets	• This argument has disappeared given vast amounts of new private capital raised
• Employee compensation & retention		X	• Less day-to-day distraction to employees due to fluctuating stock market and prices	• Any advantage not being public may have outweighed by employees’ inability to achieve liquidity on stock grants
• Investor oversight & transparency		X	• Quarterly board meetings and strong alignment of PE firms w/Mgmt	• Private disclosure often less robust than public companies, not subject to same depth of scrutiny due to narrow shareholder base
• Investor liquidity		X	• Private company shares less liquid, cannot be bought and sold except under special conditions	• Public co.’s generally have sufficient liquidity for investors to buy/sell when desired
• Asset price “risk”	Irrelevant		• Private investors often make claims that private assets are somehow more stable in value and less “risky”	• Equating market price volatility with risk is misguided and irrelevant for fundamental, long-term investors

Acronyms:

"PE" = Private Equity

"SOX" = Sarbanes-Oxley Act of 2002 mandated public company reporting, responsibility, and controls

If we agree that the parameters above reflect the primary factors driving long-term investment success, it's clear that being private is no panacea for creating superior returns. There are certainly cases in which being private is conducive to value creation – for instance, startups with evolving and unprofitable business models – but the arguments for mature, established companies cut both ways, with no clear, across-the-board advantage.

Even for startups and emerging growth companies, the more recent trend of staying private for longer (fueled by a torrent of interest in large-scale venture investing from institutional capital providers) can create valuation bubbles that defy logic. Take the recent example of SpaceX, a rocket and space transit company founded by the great 21st century visionary, Elon Musk. Founded in 2002, SpaceX has raised approximately $2.5 billion[4] over 19 investment rounds, with the most recent "Series J" fundraising appraising the company at over $30 billion, a high water mark reached in December 2018 (+10% from SpaceX's prior valuation in April 2018). Less than a month later, SpaceX has announced it is laying off 10% of its staff due to "extraordinarily difficult challenges ahead" and the need to "become a leaner company".[5] What happened in the last month, and what did Series J investors (not) know at the time of their investment?

As often happens when too much money is chasing too few investment opportunities, fear of missing out compels desirous investors in feverish assets to fling capital at targets, often without sufficient due diligence to separate facts from fiction. This phenomenon might simply be viewed as a case of "buyer beware" were it not for the contagious effects that monstrous valuation rounds can have on both private and public markets. The increasingly carnival-like atmosphere combined with limited operational and financial disclosure leaves private markets ripe for overly optimistic valuations powered by unrealistic growth assumptions. Like executive compensation packages developed by consultants, private company valuation can take on a life of its own, building up in an echo chamber that hasn't been subject to the harsh scrutiny of the public markets.[6]

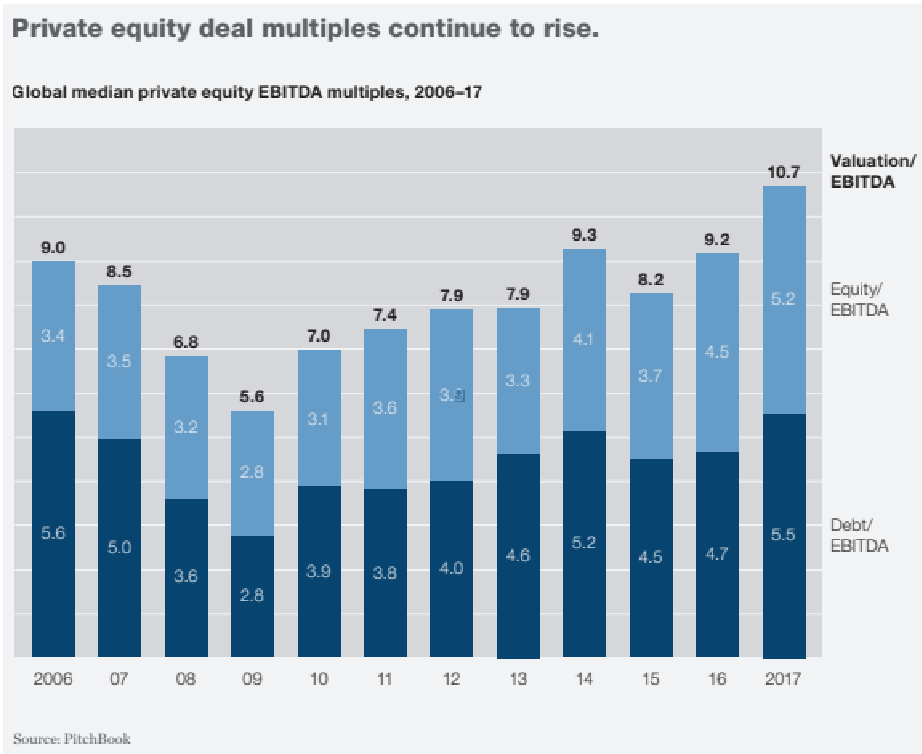
Ultimately, being private or public is largely a choice driven by the objectives of management and investors. It would be a mistake to assume that there are inherent advantages of public or private ownership that make either intrinsically more attractive To be sure, the glut of capital currently making its way to private assets is more likely

[4] "Elon Musk's SpaceX Is Raising $500m in Funding," Wall Street Journal, December 18, 2018

[5] "SpaceX plans to lay off 10% of its workforce," CNBC, January 11, 2019

[6] "Investors Beware: Today's $100m+ Late-Stage Private Rounds Are Very Different from an IPO," Bill Gurley, Above the Crowd, February 25, 2015

than not to depress private investment returns over time as deal valuations and premiums increase, eroding their margin of safety (see below).



Source: McKinsey & Company

Fortunately, Pinchot Lane Partners' small size affords the ability to invest across the entire spectrum of publicly listed assets, without having to follow the crowds currently stampeding for the greener grass of private assets. Amid headlines such as "Private Equity Seen as Top Investment for Endowments in 2019",[7] we should be thankful that the competition for public assets seems to be thinning in the wake of a tumultuous 2018.

How Hedge Funds Fared in 2018

As a category, hedge funds fared no better in the late-2018 selloff than broad market indexes; in fact, the average loss for equity hedge funds was over 200 basis points *worse* than the S&P 500 total return in 2018.[8] Marketed as superior investment products run by managers with superior pedigree and superior risk controls, these funds exhibited inferior performance against a passive index. And 2018 was no anomaly – on average this category has underperformed the index over the last decade.[9]

Beware of high-fee investment products (both hedge and mutual funds) that promise

[7] Bloomberg, December 12, 2018
[8] "Extraordinary Month Heaps Further Pain on Hedge Funds," Bloomberg, January 11, 2019
[9] "Protégé Partners Pays Up in Buffett Bet," Institutional Investor, January 8, 2018

excess returns above the index but seldom deliver. Surprisingly, many of these funds show incredible persistence long after their strategies have been discredited. Moreover, many of the larger hedge funds have opportunistically turned toward private venture investments as momentum (in both valuation and capital allocation) has shifted in that direction. In an environment where their primary strategy doesn't seem to be working, I suppose you can't fault them for trying something else.

Partner 2018 Tax Statements

Dixon Hughes Goodman, the partnership's tax accountant, is getting to work on partner K-1 statements. As mentioned above, there are some gains tax allocations to work through, but nothing unusual (except for it being the first time we've gone through this exercise). I would expect K-1s to be issued in March but will let you know if for any reason there are delays.

In Closing

The objective of our investment partnership is to produce superior returns over the long term when judged against the S&P 500. In any given year, markets can be up, down, or sideways, but the fund's investment goal is the same – to identify high quality assets at cheap-to-reasonable prices (preferably "fall over yourself cheap") using objective facts and sound reasoning. Market dislocations like the one witnessed in the fourth quarter of 2018 reveal more opportunities to find value and should be embraced even if in the short term, fund performance suffers.

As I wrote last July, the fund is nowhere close to exhausting capacity in its investment strategy. The initial investment for new partners remains $100,000, although this minimum does not apply to existing partners. Friends, family, and colleagues who share the partnership's long-term investment philosophy are welcome to join.

As usual, I invite you to let me know if there is anything unclear in these letters, if you have any questions, and/or if there are better ways to communicate with you about your partnership investment. Unless something comes up, the next letter you'll receive from me will be in July with a mid-year update on the fund's performance.

Sincerely,

Drew Peng

Attached: PLP Top 5 Portfolio Positions as of December 31, 2018
R.I.P. John Bogle (5/8/29 – 1/16/19)

Exhibit A: Pinchot Lane Partners - Top 5 Portfolio Positions as of December 31, 2018

Name	Symbol	Description	Investment Thesis	% of Portfolio Value	Date of initial investment
Hostelworld	HSW.L	Ireland-based leading global online travel agent (OTA) serving the niche hostel/backpacking market	Traded on LSE, HSW valuation declined nearly 50% during second half of 2018, precipitated by a single large shareholder exiting stake in a low liquidity environment; Company is fundamentally healthy, profitable, growing, and leads an attractive traveler niche with a highly tailored, app-driven approach	16.1%	Sep-2018
Booking Holdings	BKNG	Leading global OTA platform for travel, hotel, and other lodging accommodations with brands such as Priceline.com, Booking.com, Kayak, OpenTable, Agoda, RentalCars.com	Opportunity to own the largest, most profitable player in the OTA sector that continues to take share of $1.6 trillion global travel market, with leading positions in most developed markets excluding China; Rotated capital from EXPE to invest in BKNG during late 2018 market selloff; OTA business has demonstrated recession-resistant attributes	8.0%	Dec-2018
Alphabet	GOOG / GOOGL	Leading global search, advertising, mobile, and media platform with increasing presence in enterprise cloud, consumer devices, artificial intelligence (AI), and autonomous vehicles (AV)	Enormous growth opportunities in core product/service segments as well as emerging businesses (cloud, devices, AV, AI); trades at a reasonable valuation relative to cash flows and future opportunities	7.6%	Nov-2011
Viasat	VSAT	Provider of satellite equipment and communication services for government/defense sector, consumer broadband, and commercial aviation	Lowest cost satcom provider on critical cost per bit capacity metric; technology is years ahead of primary competitors; potential to become first truly global internet service provider post-launch of next-generation, advanced Viasat-3 satellite constellation (currently under construction)	7.5%	Jun-2012
Middleby	MIDD	A leading provider of commercial, residential, and industrial foodservice equipment with a global footprint across multiple well-recognized brands	Company has largely been built through acquisition strategy, rolling up leading brands with distinctive technologies across major equipment sub-segments, improving operations, rationalizing costs, and recently adopting a unified go-to-market approach; clear track record of creating value and growing share in a relatively fragmented global market	7.1%	Jan-2018
			Total Top 5	**46.3%**	