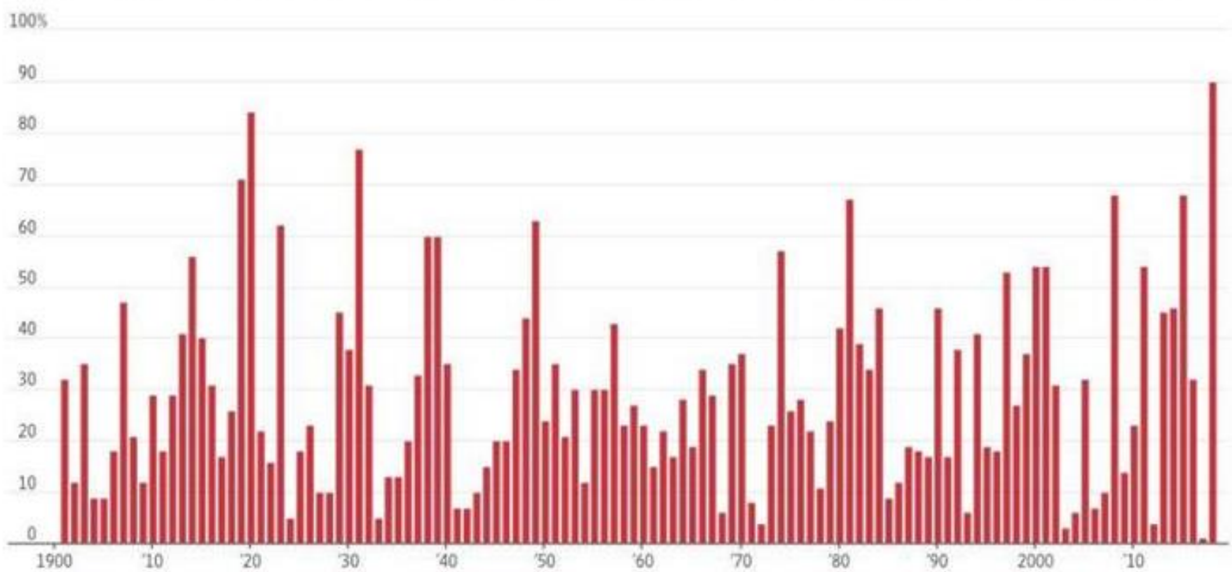
BOYLE CAPITAL

January 15, 2019

Dear Investor,

Talk about a rough year! As seen below, 2018 was one for the record books and not in a good way! More than 90% of asset classes were down for the year-worse than both 1929 and 2008.

A record share of asset classes have posted negative total returns this year, according to Deutsche Bank data going back to 1901.



Note: Returns are in U.S. dollars. Data for 2018 are as of mid-November.
Sources: Deutsche Bank; Bloomberg Finance LP; GFD

Making 2018 particularly painful was the manner in which the decline happened, with essentially all of it happening in the span of three months. The 9% decline for December marked the second worst December on record for the S&P 500 (second only to 1929) and the worst monthly decline for the index since February 2009. Put simply, what happened in the past three months was highly unusual.

While signs of a slowdown in growth have emerged, Ned Davis Research estimates that global real GDP growth for 2019 will come in at 3.5%, with estimates for real GDP growth in the U.S. at 2.75%. Historically, ***positive*** economic growth has served to put a floor in the severity of market corrections. Further, market declines do not necessarily portend upcoming economic doom. Since 1929, there have been 21 bear markets (defined as a 20% decline or greater) including the most recent decline. Of the previous 20, only 11 were associated with a recession. In other words, whether or not the current pullback in stocks is forsaging a decline in GDP is roughly a coin toss.

1230 Office Plaza Drive • West Des Moines, IA 50266 • **Phone** 515.327.1870 • **Toll-free** 877.327.1870 • **Fax** 515.619.5719 • www.boylecapital.com

At approximately 14 times 2019's (down from nearly 20 times in January) estimated earnings for the S&P 500 (and that includes some expensive mega-caps skewing the valuation higher); the market is far from overpriced. Compressions of this magnitude, going back to the 1960's, have been associated with a median stock market gain of 27% the following year. Given the decline, a lot of negative news was already priced into markets heading into January. As discussed in the following section, there are a number of bargains in the market today with many companies trading at mult-year low valuations that provide the combination of a sizeable margin of safety and attractive expected forward returns from current levels.

Company Updates

Birchcliff Energy

Shares of Birchcliff weighed heavily on portfolios in 2018, with all the decline occurring in the fourth quarter of 2018 in what can only be described as a perfect storm for energy stocks. For starters, oil prices cratered from the $70's to the $40's in a matter of weeks following the Trump administration's decision to waive certain Iran sanctions, which led to fears that we will now have an oil glut (OPEC prematurely raised production in anticipation of the Iran sanctions). The SPDR S&P Oil and Gas Exploration and Production ETF (XOP) was down more than 38% for the quarter, making it the worst quarter on record (it was down 34% in Q4 of 2008). Even though Birchcliff is predominantly natural gas, the combination of the broad market selloff and capitulation in the energy space meant virtually no one was spared. Compounding the downside pressure was year-end tax loss selling.

As stated before, not selling shares a few years back when we had the chance was a significant mistake and it has been costly. We can't undo the past, but we can learn from it and we believe we have. Rarely have shares been cheaper than they are today (see chart below), suggesting risk has been greatly diminished and returns from here should be attractive.

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
BVPS	$ 4.48	$ 4.45	$ 5.20	$ 6.08	$ 6.42	$ 6.68	$ 7.21	$ 6.65	$ 6.15	$ 6.43
Stock Price High	$ 8.85	$ 10.81	$ 15.46	$ 13.99	$ 8.97	$ 14.85	$ 9.24	$ 10.42	$ 8.81	$ 5.45
Stock Price Low	$ 3.44	$ 2.84	$ 9.17	$ 5.08	$ 6.82	$ 7.42	$ 3.45	$ 2.83	$ 3.89	$ 2.58
High (Current) P/B	1.98	2.43	2.97	2.3	1.4	2.22	1.29	1.57	1.49	0.47
Low P/B	0.72	1.76	1.76	0.83	1.06	1.11	0.48	0.43	0.62	0.40
Cash flow per share	$0.57	$0.76	$1.04	$0.88	$1.22	$2.03	$1.06	$0.74	$1.20	$1.18E
P/CF High	15.6	14.2	14.9	15.9	7.4	7.3	8.7	14.1	7.8	4.48
P/CF Low	6.0	10.3	8.8	5.8	5.6	3.7	3.3	3.8	3.3	2.6
% Change from previous low to next year high		+214%	+444%	+53%	+77%	+118%	+25%	+202%	+211%	+40%

As of 12/31/18

Figures in $CAD

Shares of Birchcliff closed the year at approximately 47% of book value and 2.6 times cash flow. On a cash flow basis, the current valuation marks the all-time low. On a price to book value basis, shares have touched near current levels (i.e. under 50% of book value) only a few other times, and as you can see, when it happened the returns from the low to the following year high was an average of 207%.

A major reason for the sharp recovery following depressed levels is the unsustainability of low commodity prices. A low-price environment sows the seeds of the next recovery and we believe we are in the midst of such an environment given the severe decline of oil prices in the fourth quarter of 2018. Consider in the past two weeks alone, Canada's oil rig count has gone from 174 to just 76, the lowest since June 2016. Here in the United States, we have already started seeing a decline in the associated gas production (natural gas that comes as a byproduct of oil production) from the Permian Basin and that trend is likely to continue throughout 2019 for several reasons. First, there are oil pipeline constraints in the Permian Basin that are likely to limit the amount of growth regardless of price. Second, as highlighted earlier, oil prices are some 40% lower than just a few months ago. Lower prices mean less revenue and less revenue means less capex spending. Lastly, there is little in the way of capital market enthusiasm for funding growth spending at current oil prices. Add them all up along with the announced cuts by OPEC and Canada and you have a recipe for lower production growth for both oil and gas in 2019. On the demand side, LNG exports from the U.S. are expected to grow from 4 bcf/d at the end of 2018 to nearly 10 bcf/d by the end of 2019. The cure for low prices has always been low prices and this time will be no different.

Despite the fact we believe shares can reach over 2 times book value as they did in 2011, 2012 and 2014, given the volatility of Birchcliff, we will opportunistically look to reduce our weighting as shares approach book value. We recognize this position has not been easy in the past 18 months, but as Warren Buffett wrote to shareholders in his 2008 letter, "when investing, pessimism is your friend, euphoria the enemy." Given the complete capitulation in everything energy over the past few months, at current valuations we are much closer to max pessimism than we are max euphoria. Despite the current valuation, Birchcliff is not a distressed company. It is generating sizeable free cash flow and is conservatively financed. Only during complete washouts do fundamentally sound companies trade at such compelling valuations. Sentiment returns, or mergers and acquisitions eventually take place. Either way, better times are ahead.

Fannie Mae and Freddie Mac

We have said it before, but it bears repeating: 2019 is the year for our investment in Fannie Mae and Freddie Mac. Even though on average we have made money on this investment to date, the past several years has seen considerable volatility as we have waited for a resolution. Our optimism heading into the new year has to do with the change in leadership overseeing the housing giants. FHFA Director Mel Watt's term ended January 6th and interim Director Joe Otting will take over the position until nominee Mark Calabria is confirmed (which could be quite a while). In a December 18th ***<u>Bloomberg</u>*** article, Treasury Secretary Mnuchin maintained his long-term position that the administration is determined to get Fannie and Freddie out of conservatorship. This was reiterated on January 10th when Otting told ***<u>PoliticoPro</u>*** that ending the conservatorship remains a priority of the administration and that "there is a clear mission that is outlined by the Treasury which includes maintaining the 30-year mortgage and completing the release of the GSEs." Otting's comments were the most specific and telling to date regarding housing reform by those in the administration. Combined with Mnuchin's frequent comments in the past about the need to protect the taxpayer and the need for any outcome to be adequately capitalized and there are only a few paths the administration can pursue as highlighted on the next page:

1. Status Quo/Do Nothing: The thinking with this option is that things are working well in housing right now so why rock the boat? Treasury is scraping $15 billion-$20 billion annually from Fannie and Freddie, so why do anything? While certainly possible (and likely the greatest risk to our investment in 2019), keeping things status quo would be inconsistent with the stated objectives of protecting the taxpayer and resolving the current conservatorship. Housing is not going to be in a positive trend forever and thus given minimal capital levels today (approximately $3 billion versus over $5 trillion in debt), any declines in the housing market are likely to be absorbed by the taxpayer. Further, and perhaps most significant, is the fact that two or three of the outstanding lawsuits will likely get to a point in late 2019 and early 2020 where an adverse decision against the government could result in tens of billions (perhaps as much as $100 billion) in damages owed by the U.S. taxpayer. If this were to happen, it would open Pandora's Box and the ability to get a resolution becomes infinitely more difficult.
2. Restructuring/Recapitalization: It is our belief that the highest probability outcome at this point is for the FHFA (directed by the Treasury) to advance a solution administratively (the likelihood of a bipartization solution in 2019 is as good as me waking up with a full head of hair!). Moelis and Company (a global investment bank with ties to both President Trump and Treasury Secretary Mnuchin) released a proposal following the midterm elections (it is not the only proposal, though we believe it be the best) that checks the box on the key issues of protecting the taxpayer by bringing in private capital and maintaining the liquidity and affordability of the 30-year mortgage. According to a December 21st ***Bloomberg*** article, "Treasury Counselor Craig Phillips has indicated in meetings with lobbyists, trade groups, academics and other administration officials that he would be amenable to parts of the Moelis plan." Something akin to the Moelis blueprint would allow Treasury to potentially earn as much as $125 billion in profits for taxpayers above and beyond what has been earned to this point (currently at $97 billion). A plan with the moving parts of the Moelis plan cannot be executed in a few months. It will take several years, and thus if the administration is focused on ending the conservatorship and capitalizing on the Treasury's investment, the time is now. The first step in restructuring Fannie and Freddie is likely requiring the companies to submit capital restoration plans. We expect this to be one of the first moves by the interim director and believe it is highly likely to occur prior to the end of March.

On September 30, 2010, AIG, the Federal Reserve, and the Treasury agreed to a recapitalization plan that would repay the Fed and centralize the government's investment with the Treasury. Over the next two years, Treasury sold its' equity stake in AIG through a re-IPO process with the last sales culminating in December 2012. The total profit to Treasury and the Federal Reserve was more than $12 billion. The preferred securities in AIG ultimately were converted to common at just under par value ($44.75 versus $45 par value).

The potential profit for taxpayers from a similar recapitalization of Fannie Mae and Freddie Mac has the potential to be ten times as large as the profits reaped by the AIG recapitalization. As for the preferred shares such as we own? Much like the AIG preferred, we ultimately expect that shares can be converted to common at something close to par value (which is what is envisioned by the Moelis plan) in a restructuring of the mortgage giants. At less than 40% of par value today (shares are up over 30% so far in January), we believe the margin of safety remains significant and thus believe it remains an outstanding investment.

Fairfax Financial

A long-term portfolio holding, Fairfax has been the epitome of a lumpy result with performance being anything but smooth or consistent over the past decade. Down 15% in 2018, shares now trade at a discount to book value and a P/E multiple under 10; making shares among the most attractive they have been in over a decade. Given sizeable cash holdings and a cheap stock price, we expect to learn in February when earnings come out that Fairfax has continued to repurchase shares over the past quarter.

AIG Warrants

Shares of AIG were down 32% in 2018. The warrants, which move disproportionate to the stock price, were hit even harder. As we wrote last quarter, we will be extremely focused on the year end results of AIG when released in mid-February. CEO Brian Duperreault has maintained they expect to exit 2018 with an underlying underwriting profit. Doing so would go a long way toward regaining confidence from Wall Street. At approximately 61% of book value, it won't take much to wake up the shares. Our warrants, which expire in January 2021, have the potential to appreciate substantially if management can put some points on the board on the underwriting front.

Bank of America

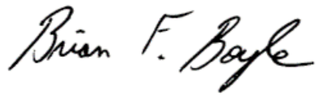
Despite surpassing 2017 earnings already in just three quarters in 2018 (we will have Q4 numbers in January and expect YoY earnings will be up close to 40%), shares of Bank of America were off nearly 15% in 2018 amid fears of a yield curve inversion and impending economic slowdown. Following the decline, shares of Bank of America are as attractive as they have been in several years. Trading around $25 per share, BAC is selling for less than 9 times estimated 2019 earnings. What's more, as communicated last quarter, Bank of America is significantly overcapitalized which means the company has been gobbling up its own shares by as much as 2% per quarter. Long a proponent of companies repurchasing their own stock when cheap, Warren Buffett must like what he sees as during the third quarter of 2018 Berkshire Hathaway purchased nearly $6 billion of Bank of America in the open market, adding to its position by nearly 30% and taking it to over $20 billion. Given their economic sensitivity, bank stocks have shown extreme volatility the past several months. While not ideal, we have seen this game before since our first purchases more than seven years ago. Long term clients have made significant gains on Bank of America and we expect the ride up (bumpy at times) to continue.

Summary

We understand the present anxiety as we are subject to the conditions-the members of Boyle Capital own what our clients own. Consider our actions as well as our words. We have been buyers. We remain confident in our understanding of these investments and are confident that their currently distressed prices will prove to be bargains. If we are right as we expect, we should see significant appreciation from today's bargain levels.

On behalf of all at Boyle Capital, thank you for your trust and confidence. We are working hard to regain lost ground. Please do not hesitate to call with any questions.

Wishing you much health and happiness in this New Year,



Brian F. Boyle, CFA

The S&P 500 is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. The index is used for comparative purposes because it approximates what an investor could earn from a passive investment in the general securities market.