April 15, 2019

Dear Fellow Investor:

It is my habit to write to you after the conclusion of each fiscal quarter to report on how things are going in the wild world of investments, both in the markets in general and in the accounts for which Weybosset Research and Management is responsible more specifically. I hope to convey our view on the state of the markets and give you some idea of our plans on your behalf. Last October I observed that Weybosset Research is a team of four individuals, each with his or her own voice, and asked Tom Lamb to take the job of reporting to you. This time around, that is, after the conclusion of the first quarter of 2019, I've asked Justin Deutsch, the new guy at our firm (he's been here 5 years), to do the job. (Stay tuned for Jeannine in July.) Take it away, Justin!
--Fla Lewis

Volatility Is Your Friend

"You do things when the opportunities come along. I've had periods in my life when I've had a bundle of ideas come along, and I've had long dry spells. If I get an idea next week, I'll do something. If not, I won't do a damn thing". Warren Buffett.

The major stock market averages continued their sharp move from the lows of December and marched higher with the Standard & Poor's 500 index closing up 13.65% for the first quarter of 2019. The markets have gone from the worst December on record to one of their best quarters in years in just a few short trading days. We are pleased with our performance so far this year, as the equity portion of the vast majority of the accounts for which we are responsible outperformed the averages, due in part to a handful of our investments making new all-time and 52-week highs - think newspapers, metering and measuring, wrecked cars, trains, and government portals.

Though last year was a disappointing year for investors, the Standard and Poor's 500 did not tell the full story of the carnage in equities for 2018. Small and mid-cap equities fared worse than the major indexes with the Russel 2000 index finishing down 12%; even worse was the performance in international and emerging equity markets. Most of the indices around the globe were down 15-30% at the end of 2018. To say that 2018 was a tumultuous year is an understatement. However nice it is to watch the major averages march higher and higher, year after year, we at Weybosset do not mind volatility. Sometimes we welcome it.

Volatility is the market's way of giving us opportunities to buy deeply discounted productive assets at reasonable prices on your behalf. To quote Warren Buffett,"… you, as shareholders of Berkshire, unless you own your shares on borrowed money or are going to sell them in a very short period of time, are better off if stocks get cheaper, because it means that we can be doing more intelligent things on your behalf than would be the case otherwise."

At the beginning of the year, you may have noticed a few changes to your portfolios. From time to time the markets provide us with mouthwatering opportunities - think banks and government services. We at Weybosset have a penchant for buying businesses for the long term, assets that will continue to make us money even when we are sleeping.

Over the years we have developed a highly efficient system with key criteria as to how we select these diamonds in the rough. Though we are astute observers of “the market” we consider ourselves business analysts rather than market analysts. Our system keeps us away from the illicit behavior of trading for short term gains. We prefer owning businesses that will compound our money for the foreseeable future. As new companies appear in your portfolios, it might be beneficial at this time to review the criteria we use to evaluate suitable investments.

1. Profitability/Growth

   We like to own profitable businesses, as profitable as possible. Not only do we want our companies to be making money in good times, but we like to see our company’s earnings per share grow during bad economic times as well. Earnings predictability and consistency enables us to understand the businesses we own for generations to come.

2. Clean balance sheets

   We at Weybosset are debt-a-phobes. If our businesses have little to no debt, then we know they cannot go out of business. I don’t know about you, but I certainly like to sleep at night. When times get tough, our companies can pull various levers to help profitability, as long as they don’t have to pay debt first…. A safety blanket while you sleep. Along with a clean balance sheet we like to see our companies routinely posting returns on capital and return on equity north of 15%. This is the ability of the company to generate market-beating returns on the money invested in their business. If a company earns very high returns year after year, then, ultimately, those will be shareholders’ returns as well.

3. Management/Ownership

   We own many different types of businesses in various sectors and in all sizes. When it comes to small and midcap companies, we like to see that the founder or management has a large stake in the company. Most people who start their own companies have the majority of their net worth tied up in the company, thus they are particularly vigilant as to what happens to their nest egg. If we are talking about large-cap companies, we like to see that the company is being run by an exceptional management team, people who have a talent for making money. We also find it of the utmost importance that management’s core values align with our own.

4. Barriers to entry

   We like to see that our consistently profitable and growing businesses have some barrier to entry; some reason that competitors cannot come in and spoil the party. Examples of barriers to entry include brand recognition - think tractors, medical supplies, and newspapers. Sometimes a company is the lowest cost provider in the space keeping competitors at bay - think access to low-cost government funds. This provides a long-lasting moat around the business and gives us a margin of safety from competition.

5. Valuation

   Lastly, and a key component of our criteria, is price. As in real estate where the keyword is location, location, location, in purchasing securities the word is price, price, and price. The price and valuation at which you purchase a company are your best offense and defense. If investors have little to no expectations that anything good could ever come from a company we are investing in, then who would be left to sell it to? The slightest change in expectations and better than expected news from a company can give way to dramatic stock gains. *You pay a high price for certainty*; that is why it is best to purchase these securities in times of distress when expectations and valuations are low. Mr. Market is a fickle spirit that from time to time may make us look foolish, unintelligent, and even devoid of creativity. But these days, as the Masters of Wall Street's time frames get shorter and shorter, they are providing us with more and more long-term opportunities to compound your capital.

The U.S economy is a strong and stable one that can take a lot of abuse. Uncertainties are inevitable, whether they derive from political or monetary policy. The one undeniable constant is the creative energy of 330 million Americans who will try to make their lives better today than they were yesterday. So, we here at Weybosset will continue to do what we have been doing for the better part of the last twenty-eight years as we see no reason to change. We continue to be highly confident in the businesses we own, and we will continue to focus on finding good businesses at bargain prices within our resilient economy. As always thank you for your trust, we look forward to protecting and growing your capital for the next twenty-eight years to come. Please feel free to contact us with any questions, comments or concerns.

Yours very truly,

Justin Deutsch
Portfolio Manager