



Value Investing With a Long-Term Perspective

Family Office GmbH

FO RUM



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Mission Statement

FORUM Family Office („FFO“) has been the vehicle to manage **the assets of a Munich-based family since 1997. FFO has no clients.**

Our mission is to invest these assets in **companies that combine an outstanding business model with strong competitive advantages into a business franchise.** When we find such companies we like to stay invested long-term, **preferably for the next generation of the family.**

We make **only direct investments and only in Europe:**

- FORUM European Smallcaps („FES“) in **publicly quoted companies**
- FORUM Private Equity („FPE“) in **privately held companies.**

We are determined **value investors:** we do relatively few investments as we:

- require a **high margin of safety**
- always perform an **in-depth Due Diligence.**



Our Values

- **The value investing philosophy reflects largely the values of the families we represent.**
The most important ones are:
 - discipline and rigor
 - thriftiness
 - responsibility
 - subordination to the requirements of a cause
 - integrity.
- The family enjoys owning companies or fractions of outstanding companies whose managers share these values and the long-term orientation. Investments in hedge funds with a 300% turnover or real estate would not be a good fit.
- We have learned that **in investing in companies these values can give us a head start, in particular:**
 - a better sense for **detecting managers with corresponding values**
 - the **internal discipline and rigor** to avoid mental biases
 - **providing long-term support**, particularly in private equity.

Persons the Family and FORUM Associate With



Friedrich II

- discipline
- service to others
- responsibility
- growth
- subordinating oneself to the state



Theo Albrecht

- discipline
- thriftiness
- simplicity as a value
- subordinating oneself to the company



Warren Buffett

- discipline
- thriftiness
- clear, rigorous thinking
- subordinating oneself to the company



1. Why Only Companies?

- Companies have the possibility to re-invest profits and cash flows internally at return rates which are not available to a financial investor. **The long-term intrinsic value of such firms can thus grow exponentially due to the effects of internal compounding. No other asset class offers this possibility.**
- All studies about the long-term performance of asset classes show that **investments in companies, especially stocks and private equity, have generated the highest returns to investors.**
- Many outstanding companies are **run by persons whose personal values fit ours**, more than those running other asset classes.

2. Does FORUM Have Preferred Sectors Or Companies?

- Any screening process **starts with the search for a one-of-a-kind business and a strong business franchise**. This almost always requires a high degree of customer retention generating recurring revenues. Such businesses have nearly always a high return on capital and can generate organic growth.
- We have **defined six industries** which we believe we understand quite well. In these industries we have a good chance to assess the risks which are created by **shifts in the overall system of markets and competition (“system risks”)**. This is our „**Circle of Competence**“.
- We observe again and again that the simpler a business model is, the higher the resulting profits. **Complexity is deadly for returns**. This is why we avoid conglomerates and complex companies.
- We do not invest in sectors or companies with risks which we can not fully assess. This includes **the whole area of technology businesses**.

FORUM „Circle of Competence“

Status as of August 31st, 2007

	Sectors with Priority	Opportunistic	Avoided Sectors
1	Brands: Goods, Services and „Verticals“. Also: Discounting Concepts	Unique Businesses with no direct competitors	Technology Companies
2	Direct Marketing, Direct Selling and Subscription-based Businesses	Specialty Finance	Telecommunication Businesses
3	Media	Software Companies	Manufacturers without After- Sales Business
4	B-to-B Service Companies		Logistics Companies
5	Manufacturers with >30% After- Sales Business		
6	Med Tech and Healthcare Services		

3. Why No Stronger Diversification?

- Other asset classes do not offer the same long-term returns as investments in companies. Therefore **a diversification into other asset classes bears high opportunity costs.**
- Our core investments in companies are **very different with respect to sector, geography and development stage.** Because we are only invested in a small number of companies, we feel that we know the risks of those companies very well. A portfolio of 20 or even 50 companies would, in our opinion, carry a higher risk **because no manager can follow and understand in-depth such a large number of companies.**

4. How Strongly Is FORUM Exposed To The Risk Of A Global Crash (“1929 II”)?

- In the case of a 1929 II event we would expect that **the survival of most asset classes is more at risk than a set of carefully chosen companies:**
 - **Real estate** because of the leverage that is employed regularly
 - **Hedge Funds** due to the associated leverage; and because of the untested default risks of derivative positions.
- Furthermore, simulations show that the correlation of those asset classes increases strongly in times of crises. We thus see only a limited possibility for real risk reduction via diversification into other asset classes.
- The companies we are invested in have strong balance sheets with barely any net leverage, but regularly a lot of cash. **They are strongly cash-generative and managed conservatively.** We are confident that **a crisis would not endanger the continuity of this set of companies.**

5. What Does “Value Investing With A Long-Term Perspective” Mean?

- We only do new investments if
 - the price we pay is significantly below the intrinsic value of the company as calculated by us, **giving us a high margin of safety**
 - the company cannot be damaged severely by external factors, i.e. there is **no risk of a permanent loss of our invested capital.**
- With listed companies we regularly see periods of significant undervaluation due to the short-term – often quarterly – perspective of financial markets. **For a value investor with a long-term perspective this offers wonderful opportunities.**
- We try to **choose our core investments in a way which enables us to hand them over to the next generation of our families (“Inheritance Stocks”)**. Our portfolio-turnover is **below 20% per year.**
- When we sell – e.g. because valuations are clearly overstretched – we are **happy to keep cash for a long time** until we have found a purchase which fits our criteria.

6. How Does FORUM Research New Investments?

- Most of our work experience lies in private equity. Between 1992 and 1998 FORUM was 100% invested in this asset class. Thus it is natural for us to apply the standards of Due Diligence common in private equity to listed companies. **Such a process can often last several months.**
- If we invest in a listed company we pretend to **buy the whole company. As such we feel that we do not own paper but fractions of whole companies.** This is one of the key principles of value investing.
- Due to these requirements we can only make in **2 to 3 new investments** per year. This number includes listed companies as well as buyouts.

7. What Role Do People Play in FORUM's Investment Philosophy?

- With each additional year in the investment business **we put more emphasis on the human aspects of business**. In our belief they are the main drivers of
 - a) the behaviour of **financial markets**
 - b) the success of **businesses**
 - c) our own success as **investors**.
- Therefore our core views on these **make us strong contrarians to mainstream financial theory**.
- Our success depends largely on understanding, recognizing and managing the **human aspects of investing**:
 - taking advantage of the **opportunities** they offer
 - avoiding the **risks** they create.

In practice we may spend ca. 75% of our time doing traditional business analysis, **but the remaining ca. 25% go into assessing people and managing our own mental biases.**

Investment Philosophy: Textbook View

Financial Theory

Financial
Markets

The value of any assets is equivalent to its discounted future cash flows

Businesses

The earnings potential of a business is determined by its sustainable competitive advantage

Investors

Active investing with outstanding brains and a defined process will generate alpha

Investment Philosophy: Human Aspects

Financial Theory

Human Aspects

Financial Markets

The value of any asset is essential to its discounted future cash flows

Markets are driven by
a) Institutional incentives & imperatives
b) Fear and greed, mass psychology
c) Short-termism

Businesses

The earnings potential of a business is determined by its sustainable competitive advantage

Managers have
a) Different skills
b) Different characters
c) Different goals

Investors

Active investing with outstanding brains and a defined process will generate alpha

Managers are hampered by a plethora of mental limitations and biases

Investment Philosophy: FORUM View

Financial Theory

FORUM View

Human Aspects

Financial Markets

The value of any asset is equivalent to its discounted future cash flows

Financial markets are inherently inefficient, regularly mis-pricing assets

Markets are driven by
 a) Institutional incentives & imperatives
 b) Fear and greed, mass psychology
 c) Short-termism

Businesses

The earnings potential of a business is determined by its sustainable competitive advantage

A manager with wrong character traits and values can devalue or destroy any business

Managers have
 a) Different skills
 b) Different characters
 c) Different goals

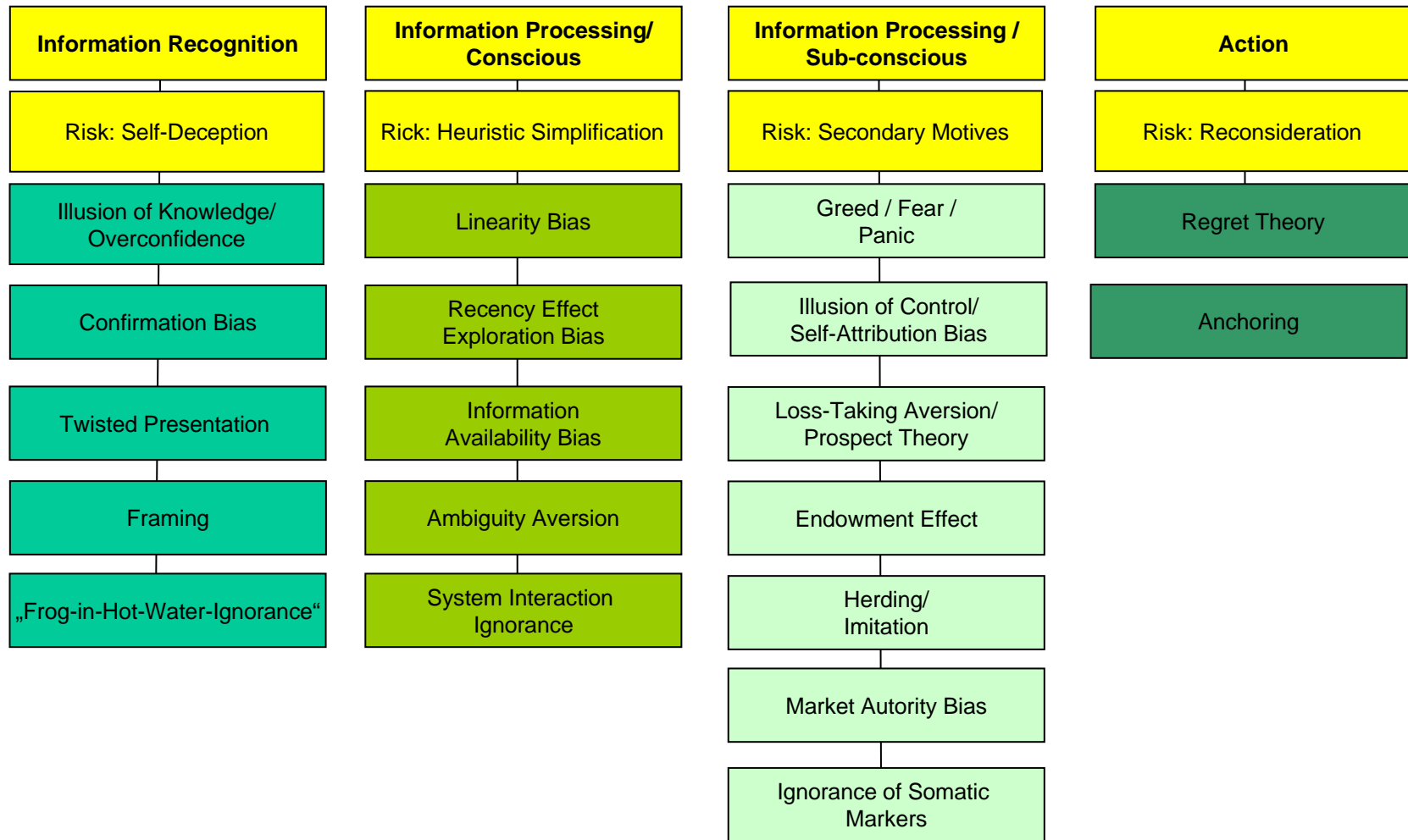
Investors

Active investing with outstanding brains and a defined process will generate Alpha

The biggest risk factors in investing are bounded rationality and lack of discipline
- WE ourselves are the biggest risk!

Managers are hampered by a plethora of mental limitations and biases

Mental Biases in Investing



8. How Does FORUM Handle “Principal Agent Issues”?

- We are very concerned about this issue. The deeper we look into the workings of institutional money management, the more we find **many players are motivated by incentive systems that do not benefit long-term investors**. The fees charged often **do not reflect the economic value added by managers**. Downside sharing is uncommon, many incentive structures are clearly **arranged asymmetrically**. **“Asset Gathering” is almost always more profitable than the maximisation of returns**.
- Therefore **we do not invest in other money managers**.
- All employees of FORUM have invested more than **90% of their wealth in parallel with our families**. Our carried-arrangement only rewards profits that are above the long-term price increase of equities. Therefore, we believe that **we have created a strong alignment of interests**.

9. What Are The Biggest Risks Of The FORUM Investment Philosophy?

- We define risk as the permanent loss of capital. Our past experience shows **that the biggest risk factors** – in order of importance - have been:
 - a) **we ourselves**: making non-rational decisions due to mental biases or lack of discipline
 - b) Deficiencies in our management system.
 - c) Inconsistencies in our investment philosophy.
- **We do not consider fluctuations of share prices a risk:**
 - a) we expect them since many highly successful value investors **had negative results up to 30% of the time**
 - b) as long as the **underlying business models of our investee companies stay intact**, their intrinsic value will continue to increase.

10. Is There A Role Model for FORUM?

- Although we will never reach his level – **Warren Buffett**. He has enhanced Benjamin Graham's concept of Value Investing with the concept of „**compounding economics**“. Buffett also invests in a **very selective way and with a long-term perspective**.
- We try to compensate for our disadvantages in intelligence and experience compared to Buffett by **focusing on European small caps**: in this segment market inefficiencies are higher than in large caps. Today, Buffett is practically limited to large caps due to the large amount of money he is administering.
- As
 - a) we have no steady inflow of float from a growing insurance business
 - b) we are small enough to be able to sell (and buy again)
we sell more often than he would do.

Dr. Burkhard Wittek, Partner



Education:

MBA, Harvard Business School
Dr.rer.soc.oec.

Career:

In total more than 30 years business experience:

- 2 years with Dresdner Bank AG
- 13 years with The Boston Consulting Group, most recently as senior partner with worldwide responsibility for the consumer goods / retail and healthcare sectors
- 10 years operating management in private equity investments of the FORUM Group
- 6 years investment management at FORUM Family Office.

Ryan Krafft, Investment Analyst



Education:

MBA. Columbia Business School



Recommended Reading

About Warren Buffett / Berkshire Hathaway

Mary Buffett / David Clark: The New Buffettology. Rawson Associate 2002

James O'Loughlin: The Real Warren Buffett. N. Brealey Publishing 2003

Robert Miles: The Warren Buffett CEO. John Wiley & Sons, 2002

About Value Investing

Kirk Kazanjian: Value Investing with the Masters. NY Institute of Finance, 2002

Bruce Greenwald et al.: Value Investing. From Graham to Buffett and Beyond. Wiley Finance, 2001

Miscellaneous

Tweedy, Browne (Publishers): Investing for Higher After-Tax Returns

Tweedy, Browne (Publishers): What has Worked in Investing



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