SeaBridge Investment Advisors, LLC

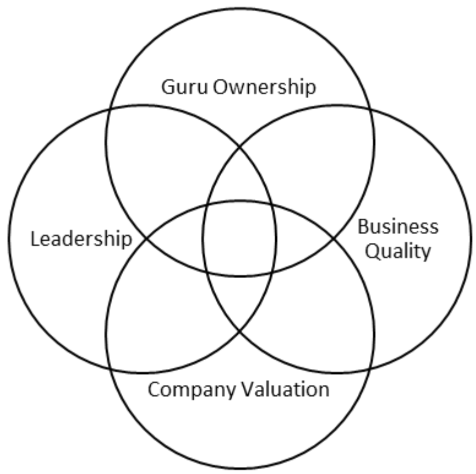
SeaBridge Longview Strategy

Second Quarter 2016

Commentary

Our Longview strategy had a weak 2Q16. It was preforming roughly in-line with the S&P 500 for the majority of the quarter. The underperformance took place in the turbulent month of June, and it is useful to see what companies got hit by the BREXIT crisis and why.

You will remember that the company analysis from CKM Research, on which Longview rests, targets the core of four overlapping Venn Rings.



Potential investments are evaluated for the following traits and typically pass at least 3 of the 4 criteria:

1. Guru Ownership: Held by one of the country's leading investment managers – those with a truly exceptional record.
2. Business Quality: The characteristic of the business seems to give it the ability to grow at double digit rates while maintaining strong gross margins.
3. Leadership: Management of the company is experienced and appears to be running the company for shareholder returns rather than egos and/or bonuses.
4. Company Valuation: At the time of purchase, it has to be both reasonable for the growth prospects and consistent with the price paid by our "guru investor."

In exploring the last quarter's performance, we focus on our major winners and losers in the Venn Ring format:

In the winner column was **Post Holdings** – the Bill Stiritz (former CEO and Chairman; now Non-Executive Chairman) roll-up vehicle for packaged foods. Mr. Stiritz compounded capital at over 50X during his 19 year transformation of Ralston Purina, and Post was to be his final creative business work. Essentially, Stiritz strategy is to leverage a stable business, and use bolt-on acquisitions and sequential steps at efficient management to grow cash flow 15+% in a business with only nominal revenue growth. In Post, the Stiritz strategy is working. A small concern, but a concern nonetheless, is that Stiritz has moved recently moved from Chairman to Non-Executive Chairman. The current CEO, Robert Vitale, stated on an earnings call that it was really just a "reflection of the reality of how we've been interacting rather than a change". So far so good, but we are thinking about how this may change the strong leadership Venn Ring.

In the minus column for the quarter is **Colfax** with a 7% loss. Colfax is the new vehicle for the Rales Brothers who are legendary for building Danaher Corp. Danaher has compounded at +20% per year since the Rales brothers gained control in 1984, and Colfax seeks to replicate their success by using the exact same playbook. The problem is that Colfax is cyclical and has much of its revenues in Europe/Russia/China. Both those factors hurt as the BREXIT crisis weakened European currencies and raised questions about a cyclical recovery. It is a fine line whether this falls within the business quality Venn Ring, or reflects the reality that many things outside the four rings are influencing the value of a company. In this case the value within the rings was overwhelmed by what was happening outside the rings. Nonetheless, over the long term, it's our belief that the Rales brothers' superior operating framework and capital allocation strategy will win out, and Mitch Rales's stock purchase of +$30 million over the last 18 months seems to support that view.

There was a lot of activity in the portfolio in our various Liberty holdings. These are led by John Malone the cable czar who has been one of the country's leading investors for decades. Various companies controlled by Malone represent over 35% of the portfolio reflecting our confidence that he is the brightest strategist in the global media scene today.

Liberty Media spun off **Liberty Sirius** (the satellite radio broadcaster) and **Liberty Braves** (the Atlanta Baseball team, related real estate and broadcast rights.)

Meanwhile **Liberty Global**, Malone's largest cable company in Europe, spun off the remainder of its interest in **Liberty Global LiLAC** – its Latin American cable company. After adjusting for the effects of the spin offs in both Liberty Global and Liberty Media, LiLAC was the biggest drag on portfolio performance. We believe that a portion of this underperformance is due to the fact that many Liberty Global shareholders received a meaningful amount of this much smaller Latin America company in the spin off, and they were either not familiar with it or it fell outside of investment managers' mandates, creating temporary selling pressure. We expect LiLAC to grow rapidly via bolt-on acquisitions and achieve the scale necessary to create a sustained advantage in the cable industry.

With all UK and EU revenues, Liberty Global itself held up very well (roughly flat for the quarter after accounting for the LiLAC spin off) given the swift devaluation of the GBP post BREXIT and uncertainties surrounding European growth going forward. Liberty Global is reported to be negotiating a joint venture with Vodafone in the Netherlands, but all the issues the EU is facing may further delay any transaction.

As with Colfax, the selling pressures hitting LiLAC after distribution are outside our Venn diagram. The net result of all the Liberty changes was roughly a negative 2% contribution to overall portfolio performance for 2Q16. As we look at each of the Liberty companies we think that cash flow is growing, and that John Malone has been an exceptional manager at getting the value of that growth back to shareholders.

Garnett Keith
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7/5/16