HAYDEN CAPITAL

Fred Liu
Managing Partner
fred.liu@haydencapital.com

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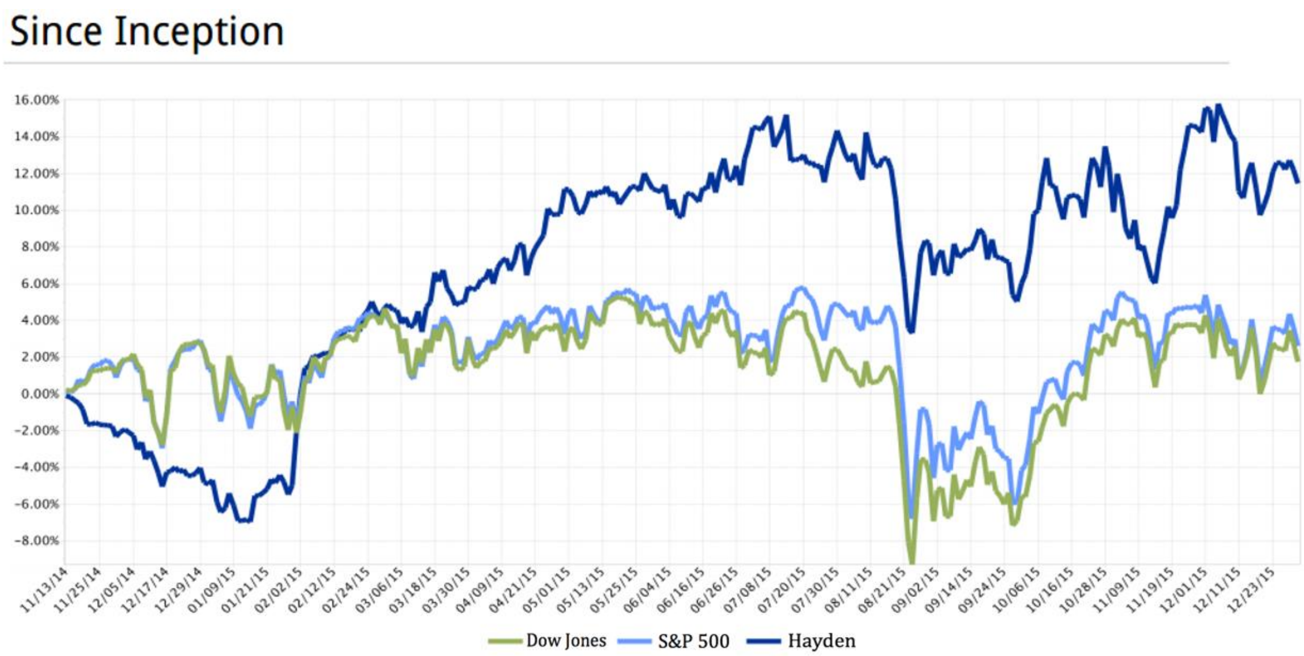
Dear Partners and Friends,

We had a great 2015. I am delighted to report that for the year ended December 31, 2015, Hayden Capital gained 17.2% versus 1.25% for the S&P 500. More importantly, we realized this outperformance despite a relatively flat market and keeping an average of 26.3% of assets in cash throughout the year.

Time Period	Hayden	S&P 500	Dow Jones	Relative Performance[1]	Avg. Cash %
			2014		
4th Quarter[2]	-4.92%	1.33%	1.52%	-6.25%	55.22%
			2015		
1st Quarter	11.16%	0.88%	0.33%	+10.28%	37.79%
2nd Quarter	6.70%	0.21%	-0.29%	+6.49%	23.32%
3rd Quarter	-6.00%	-6.42%	-6.98%	+0.42%	23.92%
4th Quarter	5.14%	7.03%	7.70%	-1.89%	20.34%
FY 2015	**17.23%**	**1.25%**	**0.21%**	**+15.98%**	**26.31%**
Total Return	**11.46%**	**2.60%**	**1.73%**	**+8.86%**	**29.74%**
Annualized Return	**10.04%**	**2.29%**	**1.52%**	**+7.75%**	**-**



While it can be pleasant to see short-term outperformance, we want to remind investors that results will vary over time, and encourage thinking about returns over a period of several years. While we are thrilled

[1] Relative performance compared to S&P 500 (Total Return). Hayden Capital returns are net of actual fees. Individual client performance may differ based on fee schedule and date of funding.
[2] Hayden Capital launched on November 13, 2014. Data reflects performance beginning on this date.

with our outperformance this year, we certainly do not expect to outperform by such a wide margin in subsequent years. However, it will not decline because of poor incentives or lack of engagement. Both my family and I will continue to have 99% of our liquid net worth invested alongside yours.

Hayden Capital Commentary

Hayden Capital was formed over a year ago, and what an exciting year it has been. With several new investors having joined recently, I wanted to take the time here to explain why I founded the firm in the first place. I know to some investors I may sound like a broken record and I have probably talked your ear off on this subject over the last year (but don't expect it to stop). Nevertheless, I feel it's necessary for all our partners to share the same philosophy and understand what Hayden Capital stands for. I promise our future letters will be more concise.

I formed Hayden Capital in November 2014, after several years of working as an equity analyst on Wall Street. During that time, I had the opportunity to see the inner workings of several institutional investment firms first-hand. And it contradicted everything I believed in as an investor. As many of you know, my investment philosophy centers around purchasing a handful of quality companies, and letting these "best ideas" cultivate over a long period of time. However, I came to realize how rare this philosophy would be in the institutional environment.

There is a myriad of reasons for why this is. Institutional mandates, regulatory '40 Act requirements on diversification, a theory among allocators that higher analyst headcounts correlate with better performance, are common justifications. Whatever the rationale may be, I believe this method of investing is flawed. So I sought to create my own investment firm, one that I would wish to invest in myself. This led to the formation of Hayden Capital.

The following are the investment values that we will seek to invest partner's capital with. Many of you have seen my musings on these topics before, but they are worth repeating. Think of this as our investing "moral code" if you will.

1. **Buy high-quality businesses for the long-term** – This one may seem like a no-brainer, but may in fact be the hardest to realize. The truth is every investor has a different definition of "quality", and I am no different (I will discuss this in detail later). However, at a simplistic level, what this means is that we believe in buying companies that will grow more valuable over time.

   We believe the value of a company tends to follow the trajectory of the underlying business value. As such, we prefer the comfort of knowing that even if we fail to purchase the stock at a discount, we will still compound our capital at the business' intrinsic return on investment capital (which presumably is attractive… or else we likely wouldn't be interested otherwise). We never hope to get lured into buying a mediocre company, despite a cheap valuation, waiting for our catalyst to materialize while the intrinsic value slowly (or rapidly) decays. This would be our worst nightmare.

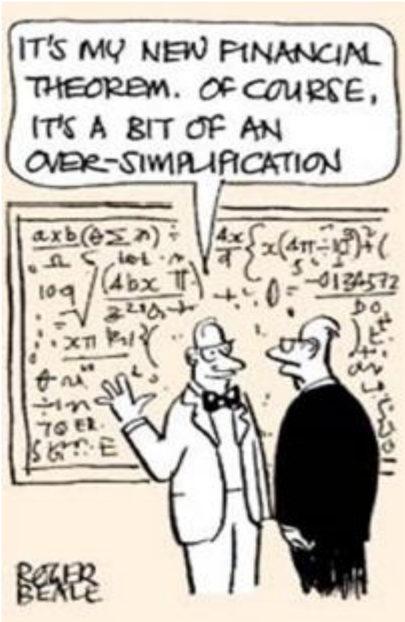
2. **Focus on underlying economic values, not stock prices –** We consider ourselves business analysts, not stock analysts. When we allocate capital to an investment, we never enter it with the goal of selling it to someone else at a higher P/E multiple or because we believe demand for shares will be higher in a few months. We make no claims to being experts at human psychology. We don't know, nor try to predict, what will be the next stock investors will want and whether they will be willing to pay more for the same business tomorrow vs. today.

   Rather, we believe that the only consistent method of making a return is to value a company based on its net cash flows over its business life, discounted by an appropriate rate. Only when a company can be purchased at a significant discount to this calculated value, should an investment be made. The difference between the first and the second method is the first relies upon the fallacy of *others* to purchase the same business at a higher price tomorrow. The second assumes other investors will be just as prudent tomorrow, and rather the business itself will grow more valuable, and thus command a higher price.

3. **Stay within our circle of competence** – This is just a fancy way of saying, "don't invest in anything we don't understand." Buffett said it best when he stated "I don't try to jump over 7-foot hurdles… I look for 1-foot hurdles that I can step over." He doesn't claim or try to know about every industry or investable opportunity. There are simply too many stocks and industries in the market. Instead, he only invests in simple to understand businesses that are within his "circle of competence", while the majority go into the "too hard" pile.

   We believe this investing mentality is wise. Likewise, you will rarely find any biotech or high-tech names in our portfolio. We simply lack the expertise to invest in these industries, and we make no pretense as to the boundaries of our knowledge. Our objective is to simply look for as many "one-foot hurdles" that we can step over as we can.

4. **Keep things simple** - Investing is more an art than a science. Too often in this industry, managers tout how their enormous excel spreadsheets or back-tested quantitative models give them some sort of edge over other investors. However, their over-reliance upon these "tools" often results in a false sense of precision, with more time wasted "data-crunching" and less time thinking. Yet investors are surprised when their managers fail to generate adequate returns.

   Instead, we at Hayden Capital don't claim to have any special tools up our sleeves. Ben Graham once said, "You don't need a scale to know that a 350 lb man is fat." We don't sweat over whether a business is going to earn $5 or $5.25 next quarter. Likewise, getting next quarter's deferred tax liability figure correct will not tell you if a business will be 3x as valuable in ten years. Instead, we would rather focus our time on determining the addressable market of the industry, what makes our company's products better (and is it sustainable), and how much effort or capital it would take a new entrant to steal our business. If you get these elements right, you'll have a much higher chance of answering that question.

   We simply try to focus on finding big gaps between the current price and a conservative estimate of intrinsic value, and are always on the lookout for that "fat" opportunity.

5. **Concentrate our capital in only our best ideas** – Our best 10 ideas are going to be better than our top 100 ideas. While we would love to invest an equal sum of money in 100 equally great companies with equally great outlooks, the markets are never going to present such an opportunity. As such, some ideas are bound to be better than others, and we will focus the fund's investments only on the best ideas.

   Similarly, the Forbes 400 list is full of individuals who put all of their chips into their single best idea (i.e. entrepreneurs). Our concentration and portfolio risk will be much lower than this extreme. However, the point is to be made that wealth is not created by investing in diversified portfolio of 100 companies of differing qualities (as many mutual funds do). Rather, differentiated results call for a differentiated approach. There is no magic number to our portfolio size, but typically, this will range between 6-15 names.

   We are also not afraid at times of holding a large cash position. Our belief is that cash not only acts as a buffer in declining markets, but it also gives us the dry powder to buy when values have bottomed. Holding cash is also preferable to investing foolishly or simply for activity's sake. Since there are no called strikes in investing, we are content to wait for that "fat pitch."

Traits of a "High-Quality" Company

Each investor has a unique definition of "quality." There are many reasons for why investors search for "quality", but the most common is that it provides a form of margin of safety. Using real estate as an example, would you rather purchase a luxury condo in an urban neighborhood, with low crime rates, and great schools? Or would you rather purchase a fixer-upper in a "bad" neighborhood, with daily shootings, no jobs, and no schools within a 20-minute drive?

Some investors would choose the latter, opting for the greater reward in return for greater risk (perhaps they believe the neighborhood will be redeveloped or gentrified soon). We at Hayden would prefer the former. Even if we paid a "fair" price for the property, we would sleep easier at night and be more confident in the likelihood of appreciation in our investment. Demand for great schools and low crime is going to be just as high decades from now, as it is today. The value of our property will grow. There is a good chance the latter property will never experience a turnaround, and the value may stay the same or even decline. After decades of declining values, even my "bargain" property may start to look expensive.

So what makes a company "high-quality"? We seek the following traits for all companies we invest in:

1. **Low Competition Risk** – Optimistically, we want our companies to be unregulated monopolies. Without competition, our business would be able to make very healthy margins, and astronomical returns. As such, we are constantly wary of the competitive landscape, and which players pose the largest threats to our business.

2. **Large Addressable Market** – We like companies that can grow their intrinsic value, preferably by selling more goods (as opposed to financial manipulation or enacting one-time cost cuts). If our business has dominant share in a large, fragmented industry, this means that there is plenty of room for our company to take market share and grow sales. The longer a business can grow at an above average rate, the more valuable it is today. If we can find such companies at an attractive valuation, this will provide more than adequate returns for investors.

3. **Healthy Balance Sheet** – The balance sheet is like the immune system of a company. During good times, a company may not need a healthy balance sheet to fend off leverage-related illnesses, and thus may not realize it has a higher chance of getting sick. However, during recessions, an impaired immune system (one caused by too much debt) may result in the mortality of a company. The majority of value in any business is in the distant future (i.e. the "terminal value"). We would certainly fail to capture this value and any of these returns in the case of a premature death.

4. **Strong Products / Pricing Power** – One of the hallmarks of a great business is one where consumers are willing to pay more and more each year for the same goods or services.

   Take the NYC Subway system for example. Millions of NYC residents rely upon the metro system to get to work and go about their business every day. Will residents really stop going to work if the city raised the fares a couple percent every year? Of course not! The city has in fact done just that, raising prices from $2 to $2.75 per ticket over the last six years. That's a 37.5% increase since 2009, or a 5.5% annual growth rate. Despite this large increase in price, the number of people riding the subway has actually gone up 12% over this time period.[3] At this rate, NYC will be able to *double* its revenues every ten years. Now that's the type of pricing power we look for!

5. **Strong, Long-term Growing Demand** – In order to have pricing power, there generally must be a growing demand for the product. It is rare for a company whose products are loved by consumers to become less valuable over time. The company can capitalize on this strong demand by raising prices, producing more units, reinvesting profits into new devices (which consumers will want even more), and perhaps even returning some of those juicy profits back to shareholders. These are all good things, and traits we like to see in any investment.

[3] The number of riders on an average weekday was 5.1M in 2009, and 5.6M in 2014. We estimate a similar growth rate for 2015.

An Investment Case Study: Cimpress (CMPR)

A recent investment that exemplifies these qualities is Cimpress (CMPR), formerly known as Vistaprint. After studying the company for close to a year and waiting for the right price, we were finally given the opportunity after shares were unfairly punished -20% after it's Q2 earnings report in late July.

There are lots to like about CMPR: a strong track record, compelling economics, an owner / operator management team that has significant ownership and makes intelligent capital allocation decisions, and strong competitive advantages that will only grow its already dominant market position.

By way of background, Cimpress helps small and micro businesses (typically less than 10 employees, and often sole proprietorships) to market themselves and look professional. They provide these businesses with a broad selection of customized physical products (business cards, flyers, banners, t-shirts, etc), as well as electronic marketing products (websites, Facebook pages, etc).

At over 100x the size of its next largest competitors, CMPR's competitive advantages (i.e. the "moat") is derived from its scale. Most costs in the printing business are fixed, and so the largest producers are typically the most profitable. This cost advantage can be seen through CMPR's gross margin profile, at 62% vs. the industry average of ~35%.

The benefits of higher margins and more items allow Cimpress to earn greater gross profit dollars per customer than its competitors. In turn, Cimpress is able and willing to spend more on advertising to attract customers, while still having plenty left over to invest in technology, the development of new products, and driving efficiency even further – something that competitors cannot match. CMPR spent $194M on research and development in 2015 alone. The average competitor had a comparatively small $14M in total revenues. How can competitors expect to compete with CMPR, when CMPR is spending 14x their total sales on continuously making their products better and more efficient?

This dynamic results in a virtuous cycle for Cimpress. Cimpress invests to attract customers. These customers lead to greater scale. More scale means more gross profit per customer. Higher gross profits per customer and more customers mean exponentially more gross profit dollars. More gross profit dollars gives Cimpress the resources to invest further, and attract even more customers, thus completing the cycle. This leads to an impenetrable "flywheel" effect and exponentially growing profits.

Four years ago, management decided to shift their strategy to reaccelerate the company's growth rate. The founder, Robert Keane, has an acute focus on growing the company's long-term intrinsic value per share, which is a function of maximizing the value earned from a customer during the customer's life. In addition, CMPR decided to focus more on the higher value, but more discerning, "high-expectation" customers. This segment of customer spends 5x more on printed marketing materials, but demands a higher quality and wider selection of products. All this would result in a higher value customer base over time, but would require increased investment and a short-term impact to margins to achieve this.

This endeavor has been very successful, resulting in 46% higher sales in the last three years (14% CAGR). Last year, management announced that after extensive analysis, they recognized there were still ample reinvestment opportunities with mid to high teen's returns that they had yet to achieve (returns well above the company's cost of capital). They had previously failed to make these investments, as they attempted to meet Wall Street's short-term expectations. Recognizing this missed opportunity, the company announced they would no longer be giving annual guidance, that future results would be more volatile, and that short-term margins would be lower over the next two years due to these increased investments. This didn't sit well with Wall Street analysts (who generally have the patience of a five year old), and resulted in a sharp drop in the share price. We started to pick up shares between $65 - 70.

We, at Hayden Capital, applaud management for having the discipline to grow the long-term value of the company, despite the short-term pain. We will happily allocate capital to companies with 15 - 20% investment opportunities. Given management's impressive track record, we don't doubt their ability to achieve this. Additionally, it seems that the management agrees with us. The company increased their share buyback after the drop, and took advantage of its lower share price by repurchasing shares themselves after the decline at ~$70.

After subsequently rising to $95 in December, shares have come back down in the recent market decline. However, company fundamentals remain unchanged and the firm has little exposure to the drivers of this latest downturn. As such, we view this as a great opportunity bestowed by Mr. Market and have been adding further to our position.

It is opportunities like Cimpress that make me so excited for the prospects of our partnership. While I expect Hayden's results to be volatile, I expect our future profits to be worth the volatility (much like the case with Cimpress). CMPR is a great addition to the portfolio, and we expect it to provide exceptional results for our partners in the years ahead.

General Musings: "Eyes On The Prize"

The objective of Hayden Capital is very simple. We simply seek to provide ourselves and our partners with more options and greater flexibility at retirement than they would have otherwise. By focusing on retirement, we believe this encourages our partners to view their investments with a longer time horizon, and allow the compounding to work its magic. For instance, take a look at the below table. It is always surprising to see how small differences in returns can add up to very significant sums over a long period of time.

If we use the 10% annual return scenario as a proxy for the S&P 500 (the index has returned about 9-11% over the last 100 years), we can see that after a short 5 years an initial $100K investment would be worth $161K. Compared to a 12% return scenario at $176K, the difference would not seem very significant. However, now let's take a longer-term view. Looking at 20 years, we can see the 12% scenario is about $300K more (or 43% higher). At 30 years, it's even more dramatic at a $1.3M difference or 72% higher. Lastly, at 50 years, the difference is astronomical, at a difference of $17M or 146% higher! All this from a $100K investment. Your kids and grandkids will surely be thankful for the smart investing decisions made by your generation.

Years Inv.	5%	8%	10%	12%	15%	20%
0	$100,000	$100,000	$100,000	$100,000	$100,000	$100,000
5	127,628	146,933	161,051	176,234	201,136	248,832
10	162,889	215,892	259,374	310,585	404,556	619,174
15	207,893	317,217	417,725	547,357	813,706	1,540,702
20	265,330	466,096	672,750	964,629	1,636,654	3,833,760
30	432,194	1,006,266	1,744,940	2,995,992	6,621,177	23,737,631
40	703,999	2,172,452	4,525,926	9,305,097	26,786,355	146,977,157
50	1,146,740	4,690,161	11,739,085	28,900,219	108,365,744	910,043,815

Warren Buffett once wrote in one of his early letters[4]:

"There are financial advantages of: 1) A long life, 2) A high compound rate, and 3) A combination of both.

[4] If you can't tell already, we're tremendous fans of Mr. Buffett's wisdom. Buffett outlined these topics in a section called "The Joys Of Compounding" in his 1962, '64, '65, and '66 partnership letters.

This explains our attitude which while hopeful of achieving a striking margin of superiority over average investment results, nevertheless, regards every percentage point of investment return above average as having real meaning."

We wholeheartedly agree with this statement. As you can see, over a long period of time, even a small difference in the annual return can have a dramatic impact on a portfolio's value. If we are able to beat the market by a mere 2-3% annually (a very realistic goal, although we obviously aim for higher), we will be able to drastically improve the financial outlook for our partners. The power of this compounding is precisely why we stress the importance of investing for the long-term, and why every percentage point is important.

Our Most Important Assets: Our Clients

One of the most overlooked facets in the success of any investment endeavor is the importance of the partners. Outstanding investors who allow us to manage our portfolio with great confidence and patient capital are truly a rare asset.

In today's industry, it is increasingly difficult to find managers who are comfortable with idleness. Maybe it is because of how the majority are measured – on a quarterly or even monthly basis. Or perhaps in an effort to seem more legitimate and bring in assets, they fill their offices with bustling staff and an aura of excitement and energy.

At Hayden Capital you'll find quite the opposite, just a quiet room with a computer, a desk, and an enormous stack of reports. We believe that ceaseless activity and insightful thought are incompatible. We're old fashioned like that. We don't find (or need) many quality ideas to produce great returns. Just one or two a year will suffice. So you'll often find us reading, thinking, and continuously learning about new industries to hone our business "toolkit." Over the years, the prices of these businesses will invariably deviate from their reasonable estimates of value. During these periods of market turmoil, we remain confident our continuously expanding intellectual toolkit will allow us to recognize and capitalize on these opportunities.

On that note, I would like to point out that Hayden Capital moved to new offices on February 1st. The new address is 79 Madison Ave, 2nd Floor, New York, NY 10016. We promise to maintain the same dull, library-esque environment our investors have come to expect.

Lastly, I just want to emphasize how appreciative we are to our investors and friends for taking part in the formation of Hayden over the last year. We value the continued support, and look forward to the next chapter of the firm.

As a reminder, we are open to new investors and introductions to potential investors are greatly welcome. Tax documents for clients will be available online and in the mail over the next few weeks.

I appreciate your continued trust in me. As it has been since inception, virtually all my family's and my own investable net worth are invested in Hayden, as we aim to compound our wealth alongside yours. As always, please feel free to call or drop by the office if you'd like to chat.

Sincerely,

Fred Liu

Hayden Capital, LLC
79 Madison Ave, 2nd Floor
New York, NY. 10016