ELGAEIAN BRADFORD
2015 LETTER TO SHAREHOLDERS

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1 Performance Comparison

Date	Elgaeian Bradford Portfolio Return	S&P 500 ETF Fund Return
1/3/2011	(0.35)	0.02
2/1/2011	0.24	0.03
3/1/2011	(0.02)	(0.00)
4/1/2011	0.10	0.03
5/2/2011	0.06	(0.01)
6/1/2011	(0.04)	(0.02)
7/1/2011	(0.04)	(0.02)
8/1/2011	0.05	(0.05)
9/1/2011	0.05	(0.07)
10/3/2011	0.06	0.11
11/1/2011	0.49	(0.00)
12/1/2011	(0.27)	0.00
1/3/2012	0.10	0.05
2/1/2012	0.09	0.04
3/1/2012	0.10	0.03
4/2/2012	(0.03)	(0.01)
5/1/2012	(0.01)	(0.06)
6/1/2012	0.54	0.04
7/2/2012	0.06	0.01
8/1/2012	(0.12)	0.03
9/4/2012	(0.07)	0.02
10/1/2012	0.90	(0.02)
11/1/2012	0.04	0.01
12/3/2012	(0.01)	0.00
1/2/2013	0.02	0.05
2/1/2013	0.11	0.01
3/1/2013	0.03	0.03
4/1/2013	0.02	0.02
5/1/2013	0.20	0.02
6/3/2013	0.19	(0.02)
7/1/2013	(0.04)	0.05
8/1/2013	0.06	(0.03)

Date	Elgaeian Bradford Portfolio Return	S&P 500 ETF Fund Return
9/3/2013	0.06	0.03
10/1/2013	0.06	0.05
11/1/2013	0.06	0.03
12/2/2013	0.06	0.02
1/2/2014	0.06	(0.04)
2/3/2014	0.06	0.05
3/3/2014	0.01	0.00
4/1/2014	(0.67)	0.01
5/1/2014	(0.75)	0.02
6/2/2014	4.96	0.02
7/1/2014	0.14	(0.01)
8/1/2014	0.04	0.04
9/2/2014	0.28	(0.02)
10/1/2014	0.01	0.02
11/3/2014	(0.20)	0.03
12/1/2014	(0.12)	(0.01)
1/2/2015	(0.34)	(0.03)
2/2/2015	(0.37)	0.06
3/2/2015	0.37	(0.02)
4/1/2015	0.27	0.01
5/1/2015	0.74	0.01
6/1/2015	(0.27)	(0.03)
7/1/2015	0.00	0.02
8/3/2015	0.12	(0.06)
9/1/2015	(0.09)	(0.03)
10/1/2015	(0.04)	0.09
11/2/2015	(0.06)	0.00
12/1/2015	(0.01)	(0.02)
1/4/2016	0.08	(0.05)

Dear Shareholders of Elgaeian Bradford Inc.,

Elgaeian Bradford is an entity practicing our understanding of irrational market by utilizing intrinsic and extrinsic value in a rational way. This year was a big change for me and for Elgaeian Bradford. We realized that we money managers need a far deeper sense of caring about our clients? interests to permeate our conduct and values. We need introspection - the most rare quality - from today?s leaders of our financial sector as well as tomorrow's. We tailor ourselves to be leaders with integrity and wisdom, leaders with a sense of history, a sense of the conditions, practices, and character of our present financial sector; and a sense of what we want our field to look like in the decades down the road.

Here is a brief list of what this letter is composed of: 1. Intrinsic Value vs. Extrinsic Value 2. Major Investment 3. Value Investing and Behavioral Finance 4. Summary of Trading Notes 5. Game Theory with Whales

2 Intrinsic Value vs. Extrinsic Value

We categorize all sorts of values into two types: intrinsic and extrinsic. Intrinsic value is a subjective concept dependent on its observer. It is a value determined by the observer and it reflects the past experiences of this observer. Extrinsic value is an objective concept referred, inferred, or reasoned from facts. Extrinsic value can almost always be found from a certain resource. Applied into stock market, the price per share can be understood as a type of extrinsic value. It is a value the market "thinks" how much a security worth. This value can be smaller or bigger than the value you think about the security. Now the key becomes very simple. A good investment is a buy at a price when you foresee major buying power ahead of your entry price. In other words, I am finding a piece of gold before the world knows that it is a piece of gold.

My first paper in 2015, published on the Homepage of corporate website, described the supply and demand in the secondary market like two forces in a warfare. It is a game between two forces and it is the accumulation/exhaustion of one force that matters the most in secondary market. My second paper in 2015 fall, also published on the Homepage of corporate website, described a research designed and conducted by myself about correlation between return of stocks and return of Retained Earnings (RE), Total Assets (TA), and ratio of Net Income and Total Revenue (NI/TR). The study shows that extrinsic value of the next period in time is highly correlated with the current intrinsic value of a stock. This explains the extrinsic value is a reflection of intrinsic value based on human psychology (fear, hope, greedy, and etc.). The understanding of the study of this paper helped us to understand a market in an analytical way and also assisted us to predict future price action with higher degree of accuracy. After that I have a series of papers published extending the same way of thinking but with more rigorous models developed to test the ideas.

As described in the opening, on one hand, we look at the future earnings power of and the broad economic moat of a company. We select target companies based on a future we understand and expect. We try to participate in the growth of companies with up trending intrinsic value, capturing the growth of alpha. On the other hand, the extrinsic value from the market can be volatile and we analyze price action to identify major buying power and selling power ahead of us, capturing the burst of beta. We discovered a link between extrinsic value and intrinsic value last year and we simply paid our greatest efforts to applying this methodology. We are creating a portfolio for our clients to capture alpha in long-term industry/sector cycle and beta in short term market volatility, hence we answer to our clients at all needs. I disagree scholars as well as practitioners to separate styles among all of the knowledges. The body of Elgaeian Bradford does not follow any style; if any, we are the style that makes money. Market nvironment is composed by different forces and any participant can suddenly jump out to form a driving force by some model. Following one style, or one model, can only hurt us more than it can reward us. I have specific corporate policies developed to prevent us into following specific styles. Only integrating everything together organically can we achieve massive amount of application in the field of investing. As a conclusion, the adaptation between intrinsic value and extrinsic value is road to seek to capture alpha and beta in the same portfolio; and it helps us to evolve to create our own water - like money managing system - we flow with the wave, sit on the whales, and capture the small fish for fun.

3 Major Investment

This year we have several major investments. None of which lies in the same industry. We are entering 2015 with a volatile start, and it was clear that the six-year bullish trend is experiencing increasing amount of selling power to continue. Market never goes flat forever. Eventually the market will give us a bigger price correction. Hence, we entered 2015 with very small beta for our portfolio.

This year we started off by taking a major position in ACT. We have Ackman behind the game and the stock has given me a clear uptrend in its course of economic activities. I do not anticipate major fail in its management team, and nor do I expect huge decrease in assets in its book. We had a stake in ACT from $257 per share. However, I made my first mistake this year that I fully liquidate the position ahead of a 5% pull-in. In order to save that 5% pull-in, I missed a 10-20% investment opportunity to the upside. This is due to my false application of intrinsic value and extrinsic value in the whole Healthcare Sector SPDR. I analyzed the intrinsic value of general biotech industry. IBB was trading at 26x its prospective earnings and 6x its book value. XBI was trading at 28x its prospective earnings and 5x its book value. Numbers here are not giving me a sell signal. Rather it is giving me an irrational buy signal or what the traders will call “chase-high”. Will this industry lead the whole economy? There is certainly a chance. However, I do not see consistent increment book value to prove that hypothesis. With that in mind, I shifted my focus away from healthcare and decided to book my profits for twenty-point profits in order to save a five-point correction. I missed another forty points after that. I am not saying I have to be perfect in each trade, but what I was doing here was a management skill leaning toward fear. This persuaded me away from standing next to our happy Mr. Market. Beta movement was captured in this stock and I was out of the position. As my fear expected, biotech did tank later this year. I am generally not on the short side of the market and we did not participate in any short selling. That being said, we caught the final small movement in one of the leading firms in biotech and we are out. This idea is again tested in the Valeant acquisition deal.

During mid 3rd quarter of this year, we took a major position in Valeant at average price of $73 per share. This position was built by the counter price activity of Bill Ackman.

We followed his steps in position. We timed the market about 3-6 weeks after his price action. Academically, we took this position based on Long-run Reversal Strategy and we are currently still in the position.

Then next major investment - Chipotle!! I have tried CMG twice this year. The first time I tried this stock was in March. The price action gave me an H-pattern to sell. When the stock failed to go down more, I acquired some position at around $660 per share. However, it made new low at $644 so I took a loss and let the stock go. I was being intellectually protective (terms to measure how heavy my positions are, from small to large: grab-and-chill, intellectually protective/defensive, intellectually aggressive/offensive, crazy-leverage) because I knew it was not a nice buy. The second time I tried was below $610 per share in July and I acquired a good amount of stocks at a monthly low price. It was the best buy I have ever done in my trading career. I managed to go intellectually aggressive. If I were crazy-leverage on this position, I could double the return. I struggled a lot, and I decided not to. There are several reasons and of course one can always find reasons against any investment. Major reasons include 1) volatility of U.S. market, 2) unsteady international political market, 3) uncertain fast-food sector cycle. I was patient and I waited for the real movement to come into this market. I had my first sell of my core position at $724, which was 110 points higher. Beta movement was captured, and I am holding the rest for alpha. Unluckily, the rest of the stock movement did not give me the alpha I expected. I got out of the rest of the position at above $630 per share. I do not see consistent growth in this stock. This is not to say Chipotle is a bad company, but some buyers are leaving the firm and we do not have that kind of buying power to support this stock. That being said, we left this position with modest amount of money made.

Tech giants GOOGL and AMZN were my third major investment this year. Two positions together summed to be intellectually defensive. I was a little uncertain about the price acquired hence I did not go heavy on any of these names. We had AMZN from $420 and I sold the stock at $487 with a beta movement. I am holding GOOGL for alpha movement.

I looked at the Gross Margin of GOOG and I ran regression between the change of price and the change of Gross Margin. The model gave me an R2 of more than 70%. Looking at the following model, we have an "outlier" after the second quarter of 2009 in GOOG?s earnings. Consistently, after the third quarter of 2011 there was another outlier in GOOG?s earnings. By saying "outlier", I am referring to a significant increase in Gross Margin, resulting a drop of R2. Economist and mathematicians will ignore this result, considering that earnings result as an number outside of prediction range interval. However, I respect the results as a fundamental change in GOOG and in time the market will digest this information.

$$r_{GOOG} = r_f + \beta\left(\frac{d(Gross\ Margin)}{dt} + \epsilon\right) \tag{1}$$

Following the same idea, I bought light in GOOG in early 2015 closed to $500 per share, a time when the Gross Margin is not doing anything. In time, I observed a significant increase in Gross Margin in the first and second earnings without any reflection of GOOG, implying a very good time to add position. I added heavy in early May around $530 and held the position all the way in July. Although Gross Margin was not the main reason, I made an investment decision largely based on this indicator and this position made my year.

The second try was a small period of COH and DOW, two names I selected to generate alpha. However, COH had bad earnings and I did not want to waste my time. DOW was not doing what I was hoping it to do. I ended up making bread-and-butter profits from these two names. Not too much of beta and alpha is captured. I failed to hold on to the positions and I left the positions with small losses.

The third position for us was in social media LNKD end of the first quarter and TWTR after 3rd earnings announcement. LNKD was a swing position rather than an investment. The name gapped down after its April earnings and we were involved with small options. However, I was unable to hold on to this position or hold the position. We broke even in this name. I held some major position for TWTR along with Dan Loeb, however I timed my position 1-2 months later than him. A lot of these hedge fund managers or activists took a position and waited for a long time before their words can be taken into actual consideration. I am still in this position at the money.

We were then heavily invested in Energy industry. This was my major loss this year. I had falsely judged the temper of Mr. Market, making a decision leaning too much on value investing. My investment thesis was in line with major reports from Morningstar and Economist. However, Mr. Market could always go lower and worse in mood. Picking a bottom is really hard especially for an industry with a negative beta. The loss was not catastrophic but it was a good amount that it took some profits away from CMG major gain.

4 Value Investing and Behavioral Finance

This section aims to discuss Value Investing along with Behavioral Finance rather than Value Investing vs. Behavioral Finance. I understand a lot of people in the industry like to talk about which ?style? it is. I respectfully disagree. Style means nothing to me. Bruce Lee said to act like water and to freely express oneself. Whatever suits the actual situation is my decision and none of these has anything to do with style.

Value investing is always the key to successful investment management of corporate finance. The ability to retain earnings will never shift away from our concentration. It never did, and it never will. This year, I have discovered another aspect of looking at financials - behavioral finance. In 2014, I tried to incorporate behavioral finance into my money management system. I did not do so because it was way too subjective. I kept asking myself “why do people trade”. All I am getting is fear and hope. I do not want anything to do with fear and hope nor can I make sound argument from them. I know it can be used as a great tool if I can understand. However, I do not think I am a master in understanding of fear and hope. I would rather look at price action and let it dictates my trades. This year we have a bridge connecting the gap between value investing and behavioral finance.

With a philosophy borrowed from Ray Dalio, this year my portfolio tracks alphas and the betas. For a certain amount of assets, a money manager should be having a promising return on certain (more than half) percentage of his account and he should also be participating with volume or momentum names with news catalyst. This is exactly what I did. For alphas, I have selected companies that pay good dividends with very little volatility. For betas, I do not hold these stocks for a long time. I trade these stocks actively like a trader. How do we differentiate these names? This is why I have Beta List and Alpha

List introduced in the following table. For stocks that I want to be participate in the market as a trader, I want to know these stocks could jump high enough for me to take a profit in short term. I will be putting on a small percentile of my assets but with bigger volatility. These are the names I will be using to generate a positive beta for my portfolio, i.e. a boost on return with market volatility. For stocks that have consistent free cash flow to pay shareholders dividend, I want to have some assets allocated in these companies to generate an alpha, i.e. a long-term return that allows me to beat market. Statistically, beta is the coefficient of the return of my portfolio and alpha is the difference when the return of my portfolio is compared to that of the benchmark taken account of risk-free rate.

One of the major improvements this year was my study of scholarly research in the area of asset pricing. With crsp/compustat stock universe in hand, I have written papers after papers to learn about as many asset pricing models as I can.

We are entering a new era, in which investors need their assets growing safely and steadily. This world is in demand of a portfolio, a world basket that is able to generate alpha and beta at the same time, a universal cash institute advising high net-worth clients and also institutional clients, and a money empire merged of virtually all ETFs available tracking the growth in each and every corner of this world. This can be done and one needs to learn from the previous scholars to accomplish this. We have pioneers sharing experience about the relation between size, valuations, and average returns on cross-sectional study (Fama, Macbeth, 1973). Not only that, we also understand momentum from De Bondt and Thayler (1985). Investors may argue previous work can be flawed. This is indeed very true and that is why we read about gross profitability premium (Novy-Marx, 2013), pointing out the lack of evidence to explain cross-section returns on Fama-French model (1992). This field is still going forward and everything comes down to serve the best interest for investors.

With an increasing understanding of asset pricing literature, I have been consistently writing papers myself as well.

I was once a very arrogant and aggressive stock trader, with thousands tier size and hundreds of thousands of shares on a monthly record. This is why some of my early papers were targeting on predicting future returns (Yin, 2013). Majority of earliest work would take time-series regression on virtually all stocks based on fundamental indicators and financial ratios, aiming to predict a certain price range with some level of significances for a particular time in the future like earnings release. This ego led me to write a paper on non-negative alpha (Yin, 2014), a purely mathematical model without any regression to look at market pric- ing model. The more I read, the less arrogant I become. I started to take compustat and crsp stock universe to conduct cross-sectional regression to study average stock returns, crunching numbers and conducting not just times-series regressions but also cross-sectional studies to look at average stock returns systematically by size and book value. The process was definitely very struggling and very painful. Hundreds of hours in the computer lab sometimes went away like wind because of an error in one of my data or matlab codes. However, it allows me to look at how different factors affect market or industries, which allows me to visually analyze the market from different dimensions. It was the paper that studies fundamental factors in different lagging time assisted me to conclude the Future-expectation Theorem ? that is, current market price takes future expectation into consideration since past and current information do not help us fully explain current price (Yin, Oct. 2015). All of these practice caused me to think big and far to create a world portfolio to track market returns. With multi-trillion dollars assets under management, the commission fee can be as low as five basis points. It will be a brand new concept with steady earnings, smaller fees, and less mental stress for everyone.

5 Summary of Trading Notes

This section collected a set of questions that I always ask myself before I put on a position.

Item	Micro	Macro
Chart	What is the chart pattern?	Why do you see this chart pattern?
Market Cycle	What is Mr. Market thinking? When will Mr. Market change what he thinks now? Why?	
Market Participants	What is the price "piranhas" want to buy?	What is the price ?whales? want to buy?
Relativity	How is this stock doing relatively to market, industry, or competitors?	Why is the stock stronger or weaker than market, industry, or competitors?
Sector or Industry	What is this sector or industry doing?	What is this sector or industry likely to do in the future? Why?
News	Is there any news?	What is majority of the investors looking for in the future? What news do they like?
Volume	What is the current volume in the market?	Who caused this volume? Why?

6 Game Theory with Whales

Remember these faces. I, as well as the Elgaeian Bradford entity, am in a game with these people.

My entries and exits will not make any sense if there is nothing to do with them. Outperforming S&P 500 is a passing grade for me, but outperforming whales will earn my reputation. (From left to right and up to down: Daniel S. Loeb - Third Point, William Ackman - Pershing Square, Stephen Mandel - Lone Pine Capital, David Einhorn - Greenlight, John Paulson - Paulson & Co., Bill Gross - Janus Capital, Daniel Och - Och-Ziff Capital, Ray Dalio - Bridgewater Associate, and Warren Buffett - Berkshire Hathaway)

As we always believed, great assets come from externally clients and internally employees. I will always be seeking the best approach to help serve our people financially. This year is a good start! From my perspective, the future goal of this company will always focus on how to manage and understand retained earnings. Hence I can be confident to transfer fiduciaries into comfortable client experiences for my people.

Best Regards,
Yiqiao Yin
Founder and President
December 31, 2015