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Del Principe | O'Brien
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Dear Fellow Investors,

Far more important than anything else, we hope this letter finds you and your loved ones safe and well. And we hope that by the time you're reading this letter, things are starting to look up.

Amidst all this uncertainty, we know one thing for certain: that Del Principe | O'Brien has the best clients on the planet. While investors around the globe were losing their collective minds in March and early April, I received calls from seven clients....and six of them were calling to put more money into their portfolios. These weren't regular IRA contributions, mind you. These were additional funds from investors like you who saw the market volatility for exactly what it was: an opportunity to strengthen our portfolio.

Kudos to you, fellow value investors, for not being scared off by Mr. Market's manic-depressive behavior. Thank you for trusting the value investing approach and remembering that it's important to ride out the short-term spikes and waves to realize long-term gains.

A Pair of Black Swans

"No amount of observations of white swans can allow the inference that all swans are white, but the observation of a single black swan is sufficient to refute that conclusion." – David Hume

Compared with previous pandemics—including the flu virus that spread worldwide from 1918-1919, which infected one-third of the world population and killed 50 million people—investors have already priced COVID-19 as one of the worst pandemics in the last century. With people being forced to stay home in order to stem the spread of the virus, many businesses in the U.S. and abroad have been brought to a halt.

As if a rapid global virus outbreak was not enough on investors' plates, another black swan landed in the pond in early March. Saudi Arabia and Russia entered an "oil price war," which led to the biggest one-day drop in oil prices since 1991 (24.1% on 3/9/20) and a decline of over 60% in oil prices since January. As a result of these simultaneous black swan events, extremely stressed equity and fixed-income investors left the market in record time. It was one of the most ferocious reactions by investors in history.

Financial panics are not totally new territory, however. Consider the 1973 oil shock; interest rates of 17% in 1982; the 1987 market crash; the 9/11 terrorist attacks; the 2008-09 credit crisis; and now the COVID-19 pandemic. Consider that the market has pulled back 20% or more 21 times since 1929. Highly disruptive events occur more often than we think, and we expect this to continue to be the case.

Handling Volatility

"For the investor who knows what he is doing, volatility creates opportunity." –John Train

In the current crisis, the S&P 500 Index declined by about 34% in 23 business days—the fastest decline of such magnitude since at least 1928. Equity volatility reached all-time highs (82.69%), exceeding the levels of the 2008-09 financial crisis (80.86%), as measured by the VIX Index. Almost every U.S. stock sold off by a massive amount almost instantly, and on average trading volumes nearly doubled.

In our view, the velocity of this decline has been partly driven by technological advancements that allow for faster trading and dissemination of news than ever before. The pervasiveness of social media likely has contributed to the speed of sell-offs, too. We also believe that many investment firms were highly leveraged and had to resort to margin calls.

During times of volatility, it's human nature to want to offload investments and get out of the market. It's painful for an investor to feel like he is "losing money" as stock prices plummet. But we value investors know better. We know that a market pullback creates opportunities. We can get into companies that we have been interested in because prices have dropped. We can strengthen our portfolio by getting out of positions that are no longer serving us. We analyze and manage risk and continue to invest for the long term, using volatility to our advantage.

Economic Moats: Mastercard and Visa

"*It is remarkable how much long-term advantage people like us have gotten by trying to be consistently not stupid, instead of trying to be very intelligent.*" *–Charlie Munger*

In our February 2020 letter, we outlined different types of economic moats, which are competitive advantages that allow a company to protect profit and maintain excellent margins over time. Efficient scale is one type of moat, and it occurs when a market is served effectively by just a few players. Monopolies, duopolies, and oligopolies are examples of this kind of moat.

Consider Mastercard and Visa. They are part of an oligopoly of major credit card networks, which also includes American Express and Discover. They are arguably the two biggest players in the market, accounting for 65-70% of worldwide payments volume, and are often thought of in tandem. Because of this moat, it is unlikely that a company could enter the market and build a network large and powerful enough to successfully erode the Big Two's profit margins.

New Purchases

"Value investing is the discipline of buying securities at a significant discount from their current underlying values and holding them until more of their value is realized. The element of a bargain is the key to the process." –Seth Klarman

Mastercard Inc. (MC) | Ownership 2%–9%

Speaking of Mastercard, the market pullback gave us a chance to become owners of this "technology company in the global payments industry." The company has been around since 1969 and with strong branding has become the quintessential household name. Mastercard generates revenues based on its customers' gross dollar volume (GDV) of activity on the products that bear the Mastercard brand—and that's a lot of activity. In fiscal year 2019, the company processed almost $5 trillion in purchase transactions. With a global market share for credit and debit cards estimated at 29% and 24%, respectively, it is the only player in the payments industry besides Visa that has a truly global presence.

The size and reach of Mastercard's network makes it essentially unassailable (See our previous section about economic moats) and has produced an impressive level of profitability. In 2019, operating margins based on net revenue were 57%. If you invested $100 in Mastercard in 2009 it would have been $1,459 in August of 2019, while the same $100 invested in the S&P would be $353. The ongoing shift toward electronic payments is yet another reason we believe Mastercard is well positioned to continue its dominance.

Visa Inc. (V) | Ownership 2%–9%

In addition to Mastercard, we are now owners of its counterpart, Visa, which calls itself "the world's leader in digital payments." Visa originated in 1958 and in 1976 became the brand we know today. Visa has almost 16,000 financial institution partners, with 3.4 billion Visa cards in circulation, and over 50 million merchants accepting Visa. In fiscal year 2019, the company processed almost $9 trillion in purchase transactions and holds more than 50% market share by purchase volume in the U.S., Europe, Latin America, and the Middle East/Africa regions. The shift toward electronic payments has aided Visa's growth, and we expect this growth to continue. On a global basis, digital payments surpassed cash payments just a couple of years ago, suggesting this growth will continue.

Like Mastercard, Visa's dominance in the market has driven its excellent profitability. In fiscal year 2019 operating margin based on net revenue was 67%. From 2009 to 2019 its operating margin has been between 56% and 67% each year, and its net margin during the same period has been between 37% and 53% each year. Consider also that in 2009 Visa's Free Cash Flow (FCF) was $252 million and in 2019 it was more than $12 billion. According to the company, if you invested $100 in Visa in

2014 it would have been $334 in September of 2019; that same $100 invested in the S&P would have been $167.

Moody's Corporation (MCO) | Ownership 1%–9%
The global risk assessment firm, Moody's, is one half of the duopoly that makes up the credit rating industry. Along with Standard & Poor's (SPGI), Moody's is the premier gatekeeper of bond ratings, with the two firms providing more than 80% of the total number of ratings issued. Moody's wide moat and intangible assets were built with not only significant investment, but also time. We view Moody's moat today as over 100 years in the making. It would take another firm decades to build the brand recognition and trust that Moody's enjoys today.

From 2009 to 2019, Moody's net margin has been consistently 25-30% each year. In 2009, its FCF was $574 million and in 2019 was more than $1.6 billion. Thanks to the recent market volatility, we now believe the company's value is worth our investment.

Portfolio Moves

"We try not to have many investing "rules," but there is one that has served us well: If we decide we were wrong about something, in terms of why we did it, we exit, period. We never invent new reasons to continue with a position when the original reasons are no longer available." –David Einhorn

Not only did the market pullback allow us to purchase new companies for our portfolio, but it also allowed us to do some necessary housekeeping. We were glad to have the opportunity to unload companies that are no longer serving us well, including Goodyear Tire and Rubber (GT), Perrigo (PRGO), and National-Oilwell Varco (NOV), and we were able to sell these stocks well before they were cut in half. In some cases, we were concerned that the companies' leadership was not delivering on their promises, which is an important aspect of analyzability. We need evidence that CEOs will make prudent capital allocation decisions, especially when times are good.

We also had the chance to add to existing investments, including Roper Technologies (ROP), Broadcomm (AVGO), Eastman Chemical Company (EMN), NXP Semiconductors (NXPI), and Berkshire Hathaway (BRK.B). These moves create a more focused equity portfolio and ensure that we are placing our hard-earned capital with companies that demonstrate great balance sheets and great growth opportunities.

JDP Bond Portfolio
While we have been using market volatility to further focus our equity portfolio, we are using this season of flux to broaden our bond portfolio to include other quality debt holdings. Over the previous five years, we have benefited greatly from our investments in the energy sector, but our Q2 2020 numbers will no doubt reflect its recent turmoil. We are keeping a very close eye on the energy sector, and like most things in life, we believe patience and due diligence will win out. It's worth noting, too,

that over the last few months, the 10-year Treasury yield has fallen to its lowest levels in history. The Fed has clearly indicated they will continue to keep interest rates low into the foreseeable future.

The following table provides a brief summary of how the JDP Bond Portfolio has performed on average over the last three years:

JDP Bond Portfolio by Quarter*

2017	Yield**	2018	Yield**	2019	Yield**	2020	Yield**
Q1	6.2%	**Q1**	7.1%	**Q1**	7.3%	**Q1**	10.3%
Q2	6.4%	**Q2**	7.3%	**Q2**	7.1%		
Q3	6.9%	**Q3**	7.8%	**Q3**	7.2%		
Q4	6.5%	**Q4**	7.4%	**Q4**	7.4%		

*Monthly yield average **Does not include redemption
(Note: We do not engage in leveraged accounts.)

What Matters

We are fortunate to be able to serve you during those times when we like what the market is doing and also when we're waiting for the tide to turn. As always, we care about your wellbeing and the wellbeing of those you care about above all else. "We're in this together" has become a cliché in the COVID-19 era, but it's absolutely the truth at Del Principe| O' Brien. We are investing our capital right alongside yours, so we are indeed in this together. Please remember, too, that we are in it for the long haul.

Thank you for your trust, especially in times like these. We will always work diligently to remain worthy of it.

Cordially,

Joseph Del Principe