

**BERIX**

# Berwyn Income Fund Commentary

**October 2017 Highlights**

- Equity and High Yield bond allocations at or near all-time lows for BERIX
- Nearly 60% of fund held in Cash and Short Term Bonds
- Willingness to be patient through high valuation period
- Conservative allocation and individual security selection resulting in muted 2017 performance

Being a contrarian value investor can be a heck of a lot of fun sometimes (mainly when markets are cheap and/or volatile). Other times, it can be downright miserable (when markets are expensive and/or exuberant). The conflict for many value investors lies in the fact that as the broad markets rally, our opportunity set of investable candidates tends to decline. Conversely, when broad markets fall, our opportunity set to add value increases. So while most people are overjoyed at the market's recent rise to all-time highs, our mood has been much more reserved. As a real time example of this dichotomy, over the past few months, the Berwyn Income Fund's allocation to the higher risk segments of our investable markets – namely, common stocks and high yield bonds – are at the lowest levels in the history of the fund.

We have been through many forms of market peaks before. We know that no amount of questioning or head-scratching will provide the answer to “why would a stock with a return on capital of ‘X’ trade at such a high multiple of earnings?”. Sometimes, the market is just willing to pay a high price for securities regardless of the risk-reward balance, yield level or earnings. The peaks and valleys throughout this valuation cycle can be interesting to say the least. But it makes very little sense to waste time whining or complaining...and there is no market condition, in our opinion, that will ever warrant making excuses for subpar performance.

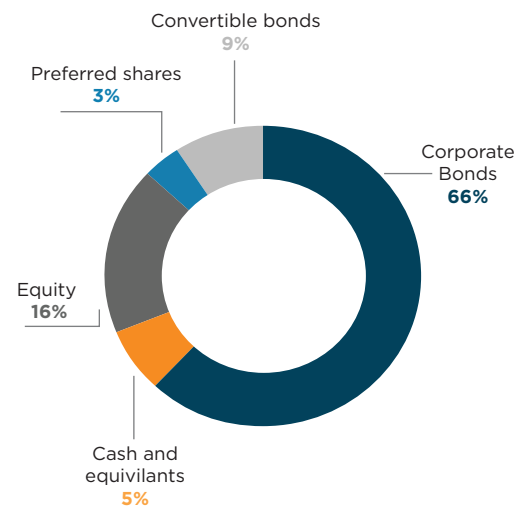
**“Don’t Whine, Don’t Complain, Don’t Make Excuses”**

*as quoted by Joshua Wooden*

Indiana farmer Joshua Wooden passed down an invaluable set of rules to his sons - Don't whine. Don't complain. Don't make excuses. The intent of this message was to teach the boys not just how to get through challenging times but also how to deal with adversity while maintaining a high degree of character. Joshua's youngest son turned out to be the legendary college basketball player and coach John Wooden. John combined rules like these and many others to develop his own special teaching and coaching style. He was so successful using this philosophical approach that he accomplished a nearly impossible feat – leading the UCLA Bruins to ten NCAA national basketball championships in the span of twelve seasons. Now, he also had his share of great players...and a lot of teams have great players. But to have an extended run of success like he did required not only great talent, but also a strong philosophical core. John Wooden certainly possessed that core. His simple but strong ethical preachings embraced values that transcended sport, work and family life. Like Joshua Wooden, many parents of adolescent children begin in earnest during their formative years to find ways to connect important life lessons through motivational conversation. After years of developing our own set of guiding principles, the effort to transfer these lessons to our kids can be difficult. They (and we) have limitations on our time together and on our attention spans. So the challenge is not just on what we have to say, but how we say it and how do we make it stick in their minds. After reading about many great teachers and people of accomplishment, the most effective lessons always seem to boil down to a message that is both simple and true. And very few are as simple or as impactful as - Don't whine. Don't complain. Don't make excuses. These rules capture the essence of personal accountability and the growth mindset. It refuses to allow any of us to fall victim to self-pity. It encourages a strong work ethic and determination. All of these attributes are required to see through short-term issues and can enable long-term success. So, just as the kids may receive this response as a retort to a complaint about a teacher or a bad grade on a test, we need to repeat these three rules to ourselves whenever we face challenging market conditions.

**Current fund positioning**

*As of 10.31.2017*



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## Don't Whine...

Today's equity and fixed income markets are, based on many measures, among the most expensive in history. The price-to-sales ratios<sup>1</sup> for the major equity indexes are at or near highs and the yields on many forms of corporate debt are at or near all-time lows. We could spend as much time as we like whining about these facts...but we will not. We will continue to attempt to add value without taking excessive risk in all market cycles.

## Don't Complain...

On an individual security selection basis, we've said 'no' to potential investment candidates about as frequently as we ever have. There is very little margin of safety in many of the companies that we research today. This combination of high valuations, low yields and little-to-no margin of safety is leading to an unfavorable balance of risk and reward in our investable universe. The fund's allocation to riskier segments of the markets - stock and high yield bonds - is as low it's ever been in the fund's history. Again, there is a tendency is to complain about the markets...but we will not. We will be patient with the confidence of knowing that markets shift and change when we least expect.

## Don't make excuses...

During 2016, BERIX's outperformance was driven by its strong security selection...but throughout 2017 nearly every significant individual contributor has been offset by a significant individual detractor. With equity and fixed income markets grinding higher, the fund seems to be running in place...one step forward, one step back. Now, our view on each holding tends to be multi-year and can extend well past any random twelve-month period. But we do from time to time make our own mistakes as we attempt to take advantage of those mistakes made by the market. Despite the fund's low allocation to stocks and high yield bonds, the kicker is that we probably should have said "no" a few more times in individual situations. Our research process and effort is sound, but occasionally poor judgment occurs in spite of our best efforts. We will not "make excuses" about any potential misstep. We will learn from each situation and carry those lessons forward in the years ahead.

## Summary

As the global stock and bond markets enjoy their rise to all-time highs, the prudence of value investing takes a back seat to the thrilling sensation of euphoria. Value investors in some cases are the spoilsports that bring up such boring and mundane topics like valuation, return on capital and margin of safety. But, as many market cycles in history have taught us, the price that you pay for a security is important; the return on capital a business generates is important; and preserving capital is critically important...all of the time, not just some of the time. As another famous American Mid-westerner likes to say, "Only when the tide goes out do you discover who's been swimming naked". With the most liquid positioning in BERIX's history, if or when the tide ever goes out for stocks or corporate bonds, the Fund will not only have its swim trunks on, but it will most likely be fully dressed. Dealing with any period of market excess can be frustrating for price-sensitive investors. But if we listen to those good, old-fashioned rules handed down by Joshua Wooden, we should be able to see through any environment with our character and capital intact.

## Glossary<sup>1</sup>

### Price-to-Sales Ratios

Valuation ratio that compares a company's stock price to its revenues.

Past performance does not guarantee future results. Investing in any mutual fund involves risk, including the risk that you may lose all or part of the money you invest. The Berwyn Income Fund invests in both fixed-income and equity securities. The Fund's investments in fixed-income securities are subject to such risks as: interest rate risk; call risk; default risk; high-yield (junk bond) risk; and unrated bond risk. The Fund also invests in equity securities which carry the potential for unpredictable drops in value and periods of lackluster performance. For additional information on these risks and other related risks (non-principal), please review the full prospectus.

**An investor should consider the investment objectives, risks, and charges and expenses of the Fund carefully before investing. The Fund's prospectus contains this and other information about the Fund and should be read before investing. The Fund's prospectus may be obtained by downloading it from the Fund's web site ([www.berwynfunds.com](http://www.berwynfunds.com)) or by calling 1-888-995-5505.**

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