VAN DIEN ASSET MANAGEMENT LLC

2014 YEAR END REPORT

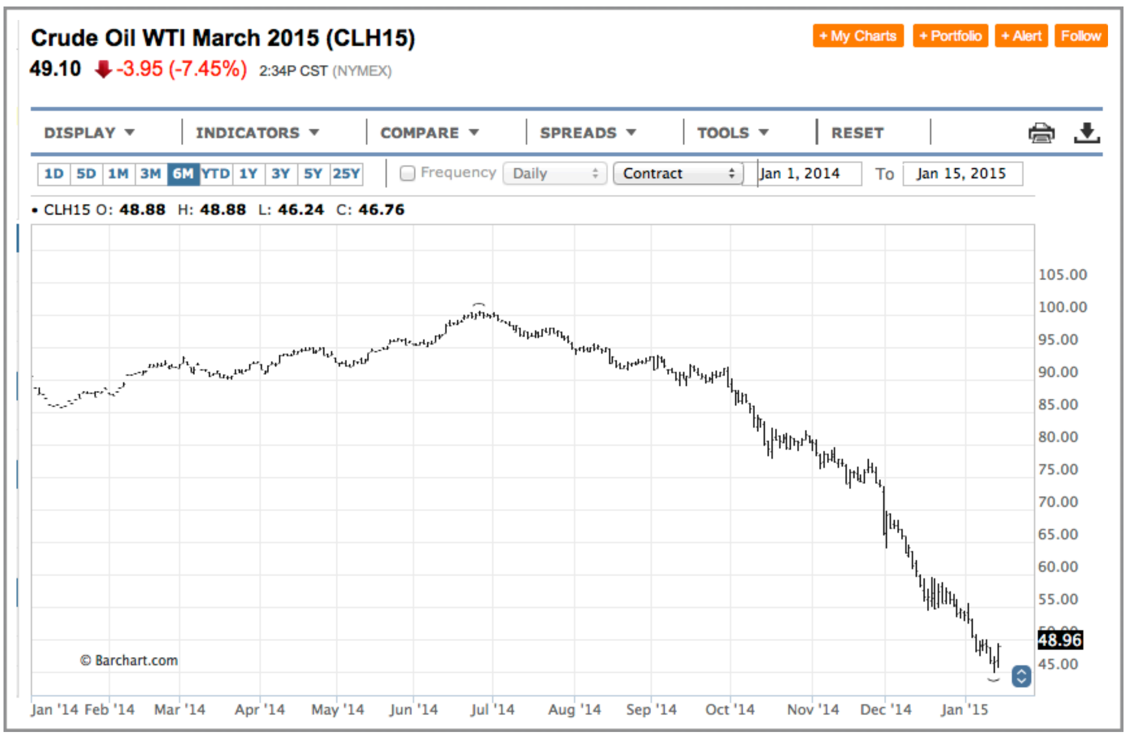
Well, Vladimir Putin and Russia certainly grabbed the headlines in 2014. Let's review a timeline of the major events. First, it was the Winter Olympics in Sochi, then Putin's annexation of Crimea in March, followed by Russia's ongoing aggression in Ukraine, the accidental downing of Malaysian Air Flight #17 by pro-Russian separatists in July, and finally the failure of ongoing diplomacy and the ratcheting up of economic sanctions against Russia by the U.S. and Europe. This sequence of events caused its fair share of unease within global markets and underscores the fragile, uncertain, volatile, and complex world in which we find ourselves living.

Of course, Russia wasn't the only source of anxiety on the geopolitical front. Investors also coped with the sudden violent rise of the ISIS (Islamic State of Iraq and Syria) extremist group, a military flare-up between Israel and Palestinians over Gaza, the rapid spread across borders of the Ebola virus, and China's seemingly increased intention to flex its own muscles on all trade and territorial disputes. Despite these geopolitical challenges around the globe, the U.S. economy continued to expand nicely.

In fact, during the second and third quarters of 2014, U.S. GDP increased at a rate of 4.6% and 5.0%, respectively, rebounding from a weather-impacted downturn of -2.1% GDP in the first quarter of 2014. The 5.0% increase was the highest single quarterly growth rate since the 3Q of 2003. While no one anticipates the economy to continue to expand at its recent torrid pace, we expect the next several quarters (including 4Q2014) to display solid growth, given the ongoing strength in the labor markets, strong consumer confidence, low inflation, and dramatically lower energy prices.

The fact is, as we enter 2015, it's the dramatic collapse in the price of oil that has garnered everyone's attention. Does the price drop signal an economic slowdown, and if so, how significant? Will the price drop cause political instability in heavily dependent oil-exporting nations, such as Russia? With copper and iron ore plummeting as well, to what extent should investors be worried about the threat of deflation? Will the inevitable energy sector job loss and bank debt write-downs cause a ripple or a wave in the U.S. economy and security markets? Can lower gasoline and energy costs give the U.S. consumer a large enough "tax cut" to offset some of these concerns? We have been studying these issues as the price of oil has tumbled.

The price of oil plunged an unprecedented 50% in 2014, and has collapsed further to the mid-$40s in early January. If this proves to be a sustained price collapse, the global economy will likely suffer. While we are not calling a bottom in oil at any particular time or price level, we do know that the seeds of its recovery are being put in place now. Capital projects are being curtailed and drillers are shutting down marginal wells. This will eventually put supply and demand into greater balance. In the meantime, drilling intensive states like Texas, Oklahoma, Louisiana and others, may see significant job losses and ultimately face some state budget issues. However, we believe that the economic benefits will ultimately outweigh any near-term disruptions. Lower oil prices has translated quickly into lower gasoline prices, in effect giving consumers the equivalent of a $125 Billion tax cut, according to Goldman Sachs economists. The middle class will see most of the benefit from these savings, since it's middle-income households that spend the most on gasoline. Also, fuel is a major expense for the food industry and for shipping almost all manufactured goods.



Additionally, an estimated 6.2 million U.S. homes rely on heating oil, most of these in the Northeast. Moody's Analytics estimates that these residents could save upwards of $3 Billion if this lower priced heating oil, now below $3/gallon, is maintained throughout the winter heating season. The silver lining for the U.S. oil and gas industry is that, ultimately, the lower priced oil may slow the usage of fracking technology to exploit shale reserves overseas, while forcing U.S. oil producers to innovate even further. Combined, these forces should serve to reinforce America's competitive lead in producing low-cost energy in the years ahead.

We often hear investment pundits fret about the duration of this bull market's run. We liken it to the top reason some portfolio managers stayed away from Apple in the 2008-10 period -- its past performance. In other words, some investors grew overly cautious on Apple simply because the stock had done so well. Yet, during this time period Apple's valuation was essentially unchanged (its share price increase was mostly attributable to earnings growth, not multiple expansion) and its growth prospects were improving as Apple developed new products and expanded into new markets. We are not suggesting the equity markets will do as well as Apple's stock. However, we do note that the valuation on the S&P 500 (currently at 1992.67) remains within reason at 16.5x 2015 estimated earnings of $120.75. Our optimism grows when considering the S&P's earnings yield of 6% (S&P earnings per share divided by the index price), which is much higher than the 1.8% current yield on the U.S. Treasury 10-Year Bond. Historically, stocks have done well when the earnings yield is 2-3x that of the yield of the 10-Year Treasury.

Performance

VDAM's composite of individual accounts finished 2014 up 9.27%, lagging both the S&P 500 which increased 11.39% and the NASDAQ which advanced 13.4%. This follows our strong 2013 in which VDAM was up 35%. Positive contributors to our 2014 performance included Apple, Yahoo!, Windstream Holdings, Time Warner Cable, and Spansion. Negative contributors to performance included Shutterfly, Cree Inc., Coherent, and Renewable Energy Group. It is interesting to note that according to data compiled by Bloomberg, the average hedge fund returned only 1.36% last year. Meanwhile, according to Lipper, the average U.S. equity mutual fund returned 4.63%. Suffice it to say that it was a difficult year to outperform the indices.

Shareholder Activism and M&A

One important theme within corporate America has been the rise of shareholder activism. Activist shareholders are building sizable positions and, with seemingly less patience than in prior years, are demanding a dialog with company managements and their Boards of Directors. We wrote about Carl Icahn's public prodding of Apple last year (see link at www.vandienasset.com) and note that Apple's stock price is up over 70% since Icahn first published his corporate criticisms. Another name we own, Riverbed Technology, has also faced the attack of a shareholder activist. Elliott Management, an activist fund run by Paul Singer, disclosed a 10% stake in November 2013 and shortly thereafter began publicly agitating for a management shake-up or sale of the firm. Elliott has had success pressuring other technology firms into shareholder-friendly sales, including networking companies similar to Riverbed, like Packeteer and Blue Coat Systems.

Our patience with our Riverbed investment was tested as management continued to stonewall Elliott's advances throughout the year, but ultimately disappointing results coupled with Elliott's increased pressure forced the Board to consider strategic alternatives. In early October Riverbed management caved to Elliott's demands and initiated a cost-cutting program and a strategic review. On December 15, Riverbed announced that it had agreed to be acquired by PE (Private Equity) firm Thoma Bravo LLC and Teachers Private Capital for $21 per share, a 39% premium to where the shares were at the time of Elliott's 13D filing (November 8, 2013, see green arrow below), disclosing its stake.

Riverbed Technology (RVBD) 09/01/2013 - 12/31/2014

In a similar vein, M&A continues to play a major role in the equity markets. As we've noted in many previous investment updates, the abundance of low-yielding cash and management reluctance to invest in large capital spending projects has many firms increasing their share repurchases and searching for acquisition candidates. Within telecom and media, AT&T showed signs of desperate determination as it tried to match scale and keep pace with Verizon which spent $130 Billion acquiring Vodafone's 45% indirect interest in Verizon Wireless. Unsuccessful with efforts to acquire both Sprint and T-Mobile USA at various turns in the past 3-4 years, AT&T eventually settled on the smaller Leap Wireless in 2013 and the currently pending $48.5 Billion deal to take over Direct TV. Not to be upstaged, Rupert Murdoch's 21st Century Fox made an attempt to purchase Time Warner Inc. that was quickly rejected. Lastly, the mega-deal that is gaining the most attention, especially from a DoJ and FCC regulatory standpoint, is the $45.2 Billion merger of cable giants Comcast and Time Warner Cable. The approval of these deals is interwoven with potential policy changes at the FCC regarding market concentration, net neutrality, and media ownership caps. We expect to hear rulings on these in the next 3-6 months.

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