MATARIN CAPITAL

Investing with Insight and Integrity

Q1 2017 Newsletter

Matarin Capital Management aspires to be a symbol of stewardship within the investment management industry. We are dedicated to delivering excellent investment performance through insight, passion, and diligence. We aim to build strategic alliances with our clients based on the highest ethical standards.
See general disclaimer on *last page.*

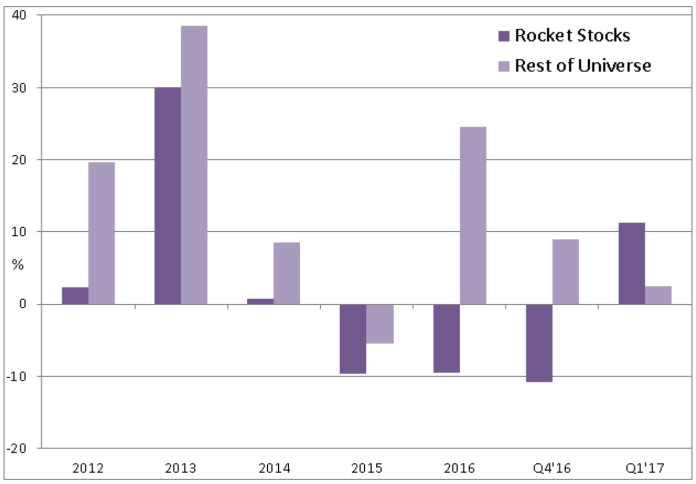
A Quarter of Anomalies, in Pictures

At Matarin, we are students of market history, and especially of proven tools for successful investing over time. A number of oddities caught our attention during Q1'17. We believe that the course will reverse in some of these dislocations, and the ensuing "return to sanity" may be bountiful for investors who are prepared. These pictures are worth a thousand words:

Speculative Stocks Rocket

"Rocket Stocks" are defined by Matarin as expensive with high growth expectations and volatile prices. Rocket Stocks have underperformed the rest of Matarin's All Cap universe by 10% annualized since 1995, but outperformed by 8% during Q1'17. We also had reason to warn of Rocket Stock rallies in 2012's The Good, the Bad, and the Speculative.

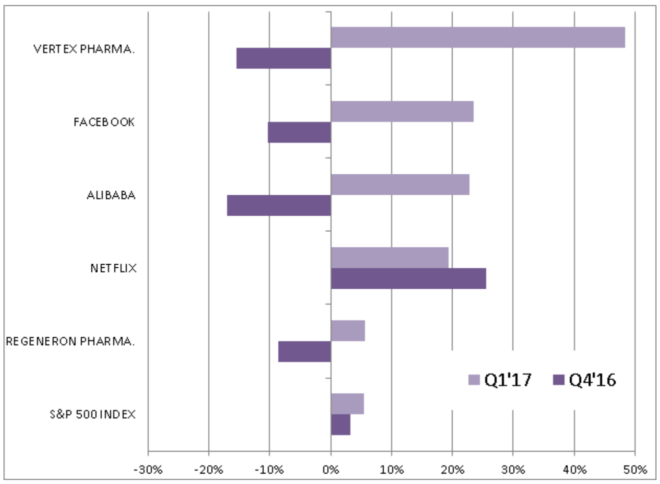
Rocket Stocks vs. the Rest of the Universe



The Rally Has Two Faces

The market rose in both Q4'16 and Q1'17, but many stocks have changed course. After the US election, Rocket Stocks were under pressure, but the most recent quarter reflected the reverse. Returns among the largest Rocket Stocks in the U.S. have turned from negative to very positive in some cases. But history shows that this trend isn't likely to last.

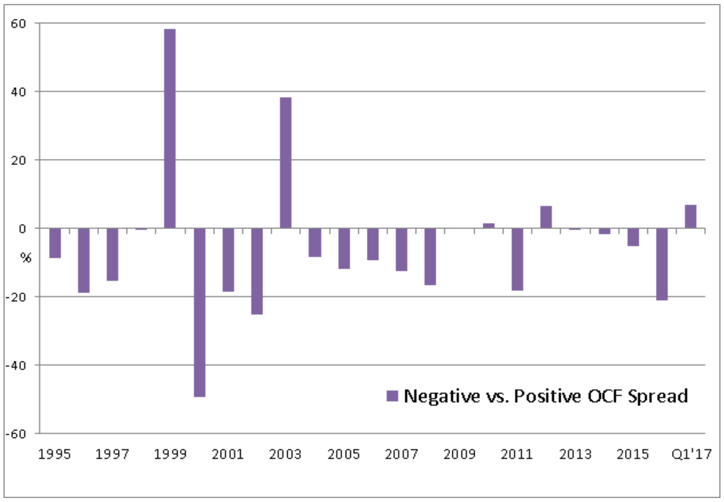
Returns of the Five Largest Rocket Stocks



Cash Burners on Fire

During only five years since 1995 have negative cash flow stocks outperformed positive cash flow stocks. On average, positive operating cash flow stocks have outperformed the negative by an annualized 10%. During 2017 year to date, negative cash flow stocks have outperformed positive by 7%.

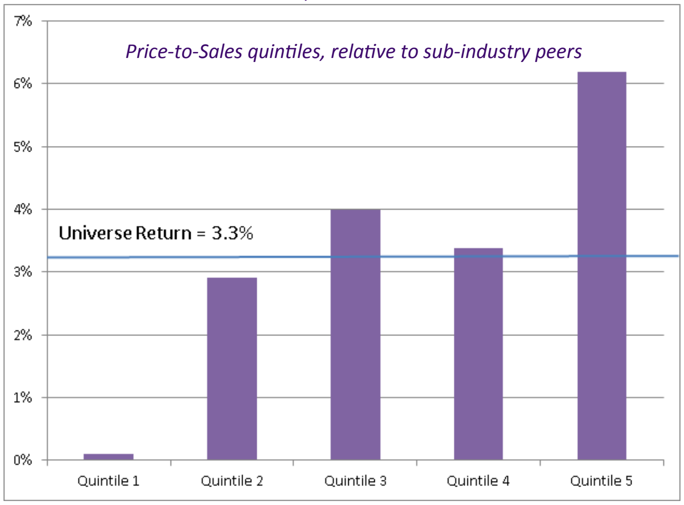
Negative vs. Positive Operating Cash Flow Spread



Expensive Tastes

During Q1'17, stocks with rich valuations rallied. Value investing works over time, but not all the time. The chart below shows Q1 returns broken down by price-to-sales, ranging from the top 20% to the bottom 20%. This inversion, with the expensive outperforming the cheap by 6% is highly unusual.

Poor on Valuation, But Rich in Q1'17 Returns



Q1 favored themes that don't work in the long run. As the market has continued its rally, it has also begun to reward more speculative stocks. The nature and tenor of the Q1 reversal makes us think it's not likely to be the *last* reversal we'll be seeing in 2017….

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