Linden Rose Investment

First Quarter 2018

Letter to LRI Clients

Quarterly Return

Quarter	**Linden Rose Investment**	**S&P 500 Index**
Q1 2018	-0.86%	-0.76%
2017	*55.51%*	*21.82%*
2016 2nd Half	*18.41%*	*7.82%*

Dear Partners:

The first quarter of 2018 started the year off with volatility and uncertainty, with Linden Rose Investment slightly trailing the broader market at (0.86%) versus (0.76%) for the S&P 500. Concern over the Federal Reserve increasing the interest rate, political turmoil in Washington D.C., and the fear of a possible trade war with China incited fear in the equity markets. As we stated in our previous letters, our relative performance in 2017 may not be sustainable and we may see some quarters with flat or negative relative performance. However, our core focus remains long-term compounded return and beating the S&P 500 index by 3-5% annually in the long run.

What Happened

We had a robust rally in January, followed by a correction in February and the resulting trend in March. The ebbing optimism over tax reform ended 10 consecutive monthly and 9 consecutive quarterly gains for the S&P 500. While our consolidated return slightly decreased in the first quarter, we welcome the recent increased volatility because bountiful returns often require more volatility.

The stock market was not and never will be straight forward or predictable. We, as value investors, would rather see price swings over a stale market. Price fluctuation is not a risk, it is a friend. It might be painful for investors who look at their brokerage accounts every hour, but for us, it provides opportunities to buy great companies at lower prices. For value investors, the joy of generating long-term profit by buying great companies at lower prices is worth the short-term pain caused by market fluctuations and Wall Street's short-term thinking.

The trick of investing is learning not to listen to your feelings. We keep hearing people say, "why are my stocks falling as soon as I buy?" Well, if you can't tolerate stock price decline or fear losing money on paper, you should not invest in the stock market at all. The most rewarded investors are those who possessed patience and sat through the ups-and-downs of the stock market. One key common characteristic of great value investors is patience. We expect uncertainties, fears, and surprises to accompany our journey for a very long time. But, as long as there is no change in the company's fundamentals, we will continue to hold our stock and not try to predict price swings. It is always essential for investors to overcome the weaknesses of our own human nature and intuition.

Keep Learning And Improving

Charlie Munger once called his pal Warren Buffett a "lifetime learning machine". We believe lifelong learning is paramount to long-term success. During the last two years of our exciting journey with our clients, we constantly reviewed our work and thought about how we could improve on a daily basis. "Diligence is the path to the mountain of knowledge". We dedicate ourselves to a continuous cycle of improvement. It is impossible to become a perfect investor who makes no mistakes, but one of our goals is to try to significantly reduce mistakes in our decision-making process. We try to become smarter everyday by compounding our wisdom.

We also want to learn from the greatest investors, for example, by reading Warren Buffett’s shareholder letters. We have read the letters several times, but we still review them and may continue to do so throughout our entire careers. Every time we read the letters, we learn something new. The biggest benefit of reading Warren Buffett's (and other fund managers) letters is that they often explain the logic behind their investments in a very clear and concise manner. When we read these letters, we ask ourselves these questions: “Why did they buy it?” and “What were they thinking about?” Over time, our thought process will evolve and develop based on what we learn and our own experiences.

Value investing involves a lot of reading. We spend at least 6 to 8 hours reading every day. Charlie Munger, also known as “a book with a couple of legs sticking out” by his children, said that: “In my whole life, I have known no wise people (over a broad subject matter area) who didn’t read all the time – none, zero.” Books are the carriers of knowledge and experience, providing necessary information about a company or an industry, and developing our minds and thought processes.

So many sages have suggested reading more, but how? Books are like the sea, never-ending. It is impossible to absorb all the knowledge found in books even if we were to read every second of our lives. An ancient Chinese poet and writer from 1,000 years ago, Su Dongpo, had some insights on this. His idea was reading with a goal. Why are you reading the book? What do you want to know? With these questions in mind, you are thinking while you are reading. Without goals or questions, the reading becomes blind.

All knowledge is cumulative. Therefore, over time, reading will make us more sophisticated, improve our investment skills, and simplify our decision-making process. The investment life may be full of contingencies, but the ultimate outcome of long-term investment is determined by accumulation.

Portfolio Updates

One major change to the portfolio was that we sold all Amazon shares for about 80% gain on average. As we wrote in our Q1 2017 letter, "Amazon is a global e-commerce company, plus AWS, the #1 global player in the fast-growing cloud business. Investing is like rolling a snowball. What you need is a long slope with very thick wet snow." Amazon is probably the company with the longest slope even if the snow doesn’t seem so thick. The quick run up of Amazon’s stock price from $1100 to around $1600 in Q1 2018 made us uncomfortable holding the shares. Even the best company can become a lousy investment if the stock price is too high. We feel the margin of safety is too thin for Amazon at the price of $1600. We wish Amazon good luck and we will buy more shares in the future if the stock price becomes reasonable again.

Another major holding worth mentioning here is Facebook. Facebook had a data privacy crisis during the quarter and the stock price sunk from $190 to $150. We took advantage of the low stock price and added a lot of shares to accounts with cash available, making Facebook the largest position in the portfolio. We did a complete and deep analysis of Facebook two years ago and we really liked the company. The combination of CEO Mark Zuckerberg and COO Sheryl Sandberg is a dream management team in Silicon Valley. Facebook owns four major social platforms: Facebook, Instagram, Facebook Messenger and WhatsApp. Out of the four platforms, Facebook is the cash machine that made most of the profit for the company. Instagram just started its monetization phase not too long ago. The other two platforms have not started their monetization phases yet. Facebook's DAU and MAU continue to grow year-over-year, even in the first quarter of 2018 amongst criticism over data privacy. Facebook had $5 billion in free cash flow and 49% year-over-year growth in revenue in the quarter. If we subtract $44 billion cash from a $500 billion market cap today, the company is selling at $456 billion, or just around 20 times this year's FCF while growing at 30-50% annually and still having two and a half platforms left for future monetization. We believe Facebook has a very long slope and very thick snow ahead.

Conclusion

Lastly, we would like to touch on a few business-related items. Our Asset Under Management ("AUM") reached an important milestone in the first quarter of 2018. We welcome and thank our new clients for the privilege of compounding your wealth for many years to come. We will keep striving to service our clients. This summer, Feng will be traveling for several weeks throughout China. During this time, Feng will be conducting some on-the-ground diligence on our current and potential Chinese investments, as well as gain a first-hand understanding of the economic trends and what is happening there. If you will be in China during this period, Feng would love to meet with you. We are very excited about the prospects of our company. While our short-term results may be volatile, we are confident that the future gains will be substantial. All our progress is still just the beginning and we will continue to grow and evolve. It remains day 1.

Again, if you have any questions about your accounts, please feel free to contact us. You can call us at (973) 841-7158 or email us at bing@lindenroseinvestment.com. If you know any friends who need investment advisory services, please refer them to us.

Stay hungry, stay foolish!

Thank you very much!

Yours truly,

Binglin Li	Feng Peng
Managing Partner	Managing Partner

May 3, 2018

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