

Once, after winning two consecutive national championships, the Green Bay Packers lost a game due to sloppy play. Coach Lombardi called a meeting the very next day. When all the players were assembled, Lombardi held a football high up in the air and declared, “Gentlemen, this is a football!” From the back of the room, running back Paul Hornung shouted back, “Coach, can you slow down?”

In investing, as in football, success is made or lost on the application of the fundamentals. This document sets forth the fundamental operating principles of Eagle Point Capital. Through the up and down markets ahead, we will always return to the principles below to inform our attitudes and actions.

- Our objective is to avoid the permanent loss of capital while maximizing the increase in long-term, after-tax purchasing power of our funds. Put another way, we aim to build an indestructible long-term compounding machine.
- To achieve this objective we seek to make concentrated investments in businesses that:
  - (1) We understand.
  - (2) Have a demonstrated and enduring competitive advantage.
  - (3) Have a resilient balance sheet.
  - (4) Have honest and able management who run the company for the benefit of shareholders.
  - (5) Can be purchased for a reasonable price that affords a margin of safety.
- In other words, we aim to purchase, at a rational price, interests in easily-understandable businesses whose earnings are virtually certain to be materially higher five, ten, and twenty years from now. We prefer cockroach-like businesses — very hardy and almost impossible to kill.
- We think independently and do our own research. We don’t rely on the opinions of analysts or journalists, both of whom may have different motivations than ours. We rely primarily on S.E.C. filings for information.
- We do not diversify excessively. Good investments are hard to come by and we would rather concentrate our capital into our best ideas than spread among many mediocre ones. We typically own six to ten businesses and put 10% of our capital, at our cost, into each.
- We think and act like business owners. As owners, we focus on the fundamentals of the business and do not obsess over price fluctuations. When possible, we use periods of unjustified pessimism to purchase high quality companies at attractive prices. Likewise, we prefer to use

periods of unjustified optimism to sell companies for more than we feel they are reasonably worth. The market is our servant and not our master.

- The best way to measure our success is to compare Eagle Point Capital's return, after fees, to the S&P 500's total return (including the reinvestment of dividends) over five-year periods. Measurement over a shorter timeframe may reflect luck more than skill. The S&P 500 is our benchmark because it is widely followed, offers the potential for large, low-cost investments, and, we expect, will produce satisfactory long-term returns. Over time, we expect good relative returns to the S&P 500 to become excellent absolute returns.
- All accounts are managed *pari passu*. Clients may elect one of two fee structures:
  1. A two percent annual fee on assets under management charged quarterly in arrears.
  2. 25% share of profits in excess of a 6% hurdle rate, subject to a high water mark, charged annually in arrears. This option carries no management fee.
- Clients will receive a letter twice a year detailing what they own and why they own it. Our reports will be candid, emphasizing the positive and negative factors important to appraising intrinsic business value. Our guideline is to tell you the business facts we would want to know if our positions were reversed. We owe you no less.
- Eagle Point Capital is not in the business of predicting the general stock market or business fluctuations. If you think we can do this or that it is essential to an investment program you would be best suited looking elsewhere.
- We cannot guarantee results to clients. What we can and do promise is that:
  - Our investments will be chosen on the basis of value, not popularity;
  - We will attempt to bring risk of permanent capital loss (not short term quotational loss) to an absolute minimum by obtaining a wide margin of safety in each investment; and
  - We have virtually our entire net worth invested alongside Eagle Point Capital's clients. We eat our own cooking.

Many of you who are already familiar with Eagle Point Capital may feel, like Paul Hornung, that this material is unduly repetitive. However, we would rather have many bored clients than a single client with any basic misconceptions. As Charlie Munger says "A majority of life's errors are caused by forgetting what one is really trying to do." A firm grasp of our fundamental operating principles will help us stay the course in the future.