

**SUMMARY OF 2003 AND A CONVERSATION WITH MR. MARKET
JANUARY 2004**

Dear Investors,

- At 30 January 2004, Sextant PEA had €38 million of assets.
- Sextant Grand Large had €4 million.

Although our assets have grown considerably since the start of 2003 (when they were €6.5 million), they are still quite modest (0.03% of the total assets managed by equity mutual funds in France!).

- In 2003, Sextant PEA gained 64%, outperforming the index by 48%, while Sextant Grand Large has increased 14% since its launch in July. On the superb Boursorama website, under “Sicav & FCP > Palmarès,” you can see that PEA is one of the best-performing funds in the world for 1-year and 2-year returns, in the company of funds from India, Thailand, etc.
- For 1-year returns, PEA is neck-and-neck with tech funds, but tech funds plummeted 50% in 2002, while PEA rose 14%. Sextant PEA is not a tech fund (fortunately for you), but if tech stocks are undervalued, we know how to take advantage of them.
- For the past 2 years, the second-best mutual fund eligible for PEAs (French equity savings plans) has risen 40%, well behind Sextant PEA, which has soared 100%. Now be honest, that’s not too bad, is it?

2003 Management Report

The key items were covered in our 2002 Report, which the bravest amongst you can read again. We basically wrote what were going to do, then did what we wrote. So rather than copying the same text and changing a few dates and commas, (the 2002 report is available on our website), I would rather use this opportunity to recount the conversation I had recently with my dear friend, the very kind Mr. Market.

Mr. M: Hello François!

Mr. B: Uh...Hello Georges.... (Georges can be a bit tiring at times).

Mr. M: 65% return on PEA and 14% on Grand Large. Well done, Admiral!

Mr. B: The Admiral is in Brittany, you know that, I’m only the navigator.

Mr. M: Yes, I know. With your Sextant, you measure companies’ values. I regret not having invested in your Funds. But come now, it’s much easier to manage five million euros than several hundred like the fund managers at my bank.

Mr. B: Yes, you are right. That is why you are staying with them...

Mr. M: Okay, but your assets are growing. You can’t keep this up forever.

Mr. B: Listen, Georges, I was alone when I managed €5 million, but soon there will be four of us to manage €40 million. I don’t know that we will always do this well, but at least we are giving ourselves the resources!

Mr. M: True, but I am not so sure that is a good thing. The best fund managers work alone; that's what everyone says. Just look at your role model, Warren Buffett.

Mr. B (inspired by Walter Lippmann): When all men think alike, no one thinks very much, Georges.

Mr. M: Okay, okay, I know, don't follow the herd. But today, internet stocks are all the rage, and you are riding the wave just like everyone else.

Mr. B: Yes, just like everyone else I use the internet more and more, but I visit fewer and fewer sites.

Mr. M: The problem, François, is that there is no cash in these small-caps.

Mr. B: True, we need to be patient. It could take a few months to build a nice holding.

Mr. M: And you are artificially boosting the stock prices!

Mr. B: Artificially, I don't know. But yes, we are lifting the prices. For example, I "lifted" Ubiquis at €2.4, and Business Interactif at €0.80.

Mr. M: See, I knew it. So how did you exit your positions?

Mr. B: With Ubiquis, I waited until a buyout offer at 4.2, which happened in early 2003. With Business Interactif, I cashed in a €1 extraordinary dividend, then sold at 1.4 in a few days. Oddly enough, when the price goes up, volume goes up too.

Mr. M: Ah, right.

Mr. B: Good-bye, Georges.

Yes, my dear Walter, "when all men think alike," at Amiral Gestion we immediately ask ourselves if it wouldn't be better to think different (in stock markets, there are only two directions, it's fairly straightforward). Actually, that's not exactly right. To take Lippmann a bit more literally, "when all men think alike," at Amiral Gestion, we ask ourselves if we shouldn't just simply think (which often means the same thing for those who are still with me, but I am beginning to have a hard time understanding myself!). So instead of listening to me philosophise (I got a 2/20 in my philosophy course), perhaps you would prefer I talk investing?

2003: A summary of our activities

As I explained earlier, in 2003 we benefited from:

- The internet rocket coming back down to earth at the end of 2002/early 2003, then taking off again and soaring until now (Auféminin.com, Business Interactif, LDLC.com, Nomatica, Medcost, Ad Pepper Media, Lycos). These stocks have absolutely exploded. We didn't understand anything about internet stocks in 2000 (was there really much to understand at that point?), and missed the boom and bust, but have since caught up by working hard.
- The extremely undervalued industrial stocks in early 2003, for companies in a fair amount of debt, but with strong cash flows (IMS, Otor).
- The year's buoyant M&A activity, with low transaction prices and significant leverage (Toupargel, Pharmagest).³

- The turnaround in the CAC 40 in March/April (thanks to Renault and Carrefour).
- The delayed panic surrounding mad cow disease (Buffalo Grill).
- The amazing work of the employees at Neurons and SII, who bravely held fast through the storm that shook IT services.
- And of course, the successes of our favourite stores, Camaïeu, Gifi, and Vet'Affaires.

Most of all, however, we benefited from the excellent quality of the managers that we had the pleasure to meet.

2004: The year of ADLP

We have already spoken to you about this company, which we bought for the first time at €10 in 2002, and whose share price today is.... €10. After dipping down to €5 at the beginning of 2003! Indeed, a thrill for us, as we are staunch believers in “He who loses, wins” (see our newsletter of the same name). We believe this company’s share price will at least double in two or three years (but be warned, anyone can make a mistake; it could be in two or three weeks). We have a 10% stake in ADLP. This would be a good time to explain a bit about how we operate.

ADLP sells short-term subscriptions (which in French is abonnements à durée limitée, or ADL) through partners (P). For example, I am a Crédit Lyonnais customer, and every year the bank sends me a brochure offering several magazine subscriptions (the choice is huge) at rock-bottom prices (discounts of 20% to 40%). The payment is deducted automatically from my debit card (I don't have to do a thing) and I can cancel anytime. You have no doubt received the same brochure, and you have no doubt binned it, as I did for several years. But one day you will realise that it is a very useful service, and that is rather enjoyable to read Gala or Paris Match in a place other than your Thai acupuncturist's waiting room. So, point number one, I understand the product (okay, so that did not exactly take a stroke of genius), and I find that it is a real service to consumers (which anyone who has wasted two years on a subscription to a useless magazine can attest to). It's easy to cancel subscription or start a new one; all it takes is a simple phone call. In fact, why don't you give it a go yourself? Call +33 08 92 68 10 98 (call now!), and subscribe to whatever you want. If you have an account with a major bank or a Carrefour Pass card, it should work.

Everyone is happy; you, your bank (your debit card gets a workout), and the magazine publishers. There are no competitors. It's a business that has high start-up costs and high barriers to entry. You have to spend a lot of money, and you only get a small return. But for a long time. You must be willing to invest for at least five or six years before seeing any cash come in.

Key figures

Number of shares outstanding: 2,410,000. Share price: €10. That gives a market cap of €24 million. No debt at the end of 2003 (or almost no debt). Net earnings in France: €3 million in

2002, and I predict at least €3.5 million in 2003. Therefore the P/E ratio is 6.8. Sales grew 16% in France. But in 2002, ADLP lost €3.3 million in its international businesses; Germany came to a halt, as did growth in the UK and Spain. So a loss in 2002 and not more than breakeven expected for 2003.

ADLP had 1,550,000 active subscribers at the end of 2003, up 20% from the previous year. The company recently announced that it sold 37,000 subscriptions in Germany for €1,500,000, or €41 per subscription. $€1,550,000 \times 41 = €63$ million. That is a market cap greater than €24 million, no? This is what I call a good safety margin. In addition, ADLP shouldn't only reach breakeven in 2003, but be highly profitable, because it recorded a last-minute capital gain at the end of December (subscriptions are not valued as assets).

Of course, anyone can make a mistake, and the stock could drop by half or triple. You will see. You and Mr. Market, whom I hope will soon buy ADLP at €40 (which might even turn out to be a bargain).

2004: More risks than 2003

We don't like risks. Unlike what people tell you, the less risk you take in the stock market, the more you earn. People confuse the risk of not matching the index with the risk of losing money. For us, underperforming an index is not a risk; losing money is. As 2003 began, our risk was incredibly low. For example, Business Interactif: stock price €1; fourth quarter cash EPS of €1.6; €0.40 loss carry-forward. If it works, we make money; if it doesn't work, we make money. Risk = 0. We like that, but it only happens once every 30 years.

In 2004, there won't be any investments quite this easy. For example, we are shareholders of an internet project that lost money in 2003. If it works, we make 10X; if it doesn't work, we lose 50%, or even 100% (well, to lose 100%, it would have to completely bomb). But we think that the probability of it working reasonably well is 25%, very well, 50%, not well, 15%, and not at all, 10%. So our positive expectancy is: $50\% * 900 + 5\% * 100 + 15\% * (-50) + 10\% * (-100) = 367.5$, for an initial investment of 100. This means we have a 50% chance of making 900 (i.e., 10X), a 25% chance of making 2X, a 15% chance of losing half, and a 10% chance of losing it all. At these odds, I would bet every day. (At a casino, the expectancy is negative; betting on red, for example, has an expectancy of $1 * 18/37 + (-1) * 19/37 = -0.027$, because you win on 1 out of 18 numbers and lose on 1 out of 19 numbers. No matter, I hate gambling at the casinos).

So in conclusion, your Funds will probably go up less in 2004 than in 2003, because the market will correct valuation errors more slowly; errors that are not quite as glaring as they were in 2003 (Business Interactif, that was screaming at us). The safety margins are less impressive. But they are still high enough for us to invest 55% of Grand Large in equity.

Grand Large in 2003

In 2003, Grand Large was invested in only 6 companies, for an average equity exposure of 45%. But the Fund has gained almost 30% since July. This is further proof that our management style, based on a concentrated portfolio, works. Our best picks performed better than others, and we were wise to concentrate on them. The market risk is much lower in Grand Large than in PEA, because Grand Large still has almost 50% cash, but its company risk is higher, because it is more concentrated. Given that we are not masters of market risk, we are happy to see it decline. But we can control the risks that we take on companies. If we lose, we can only blame ourselves, whereas if PEA drops, we can always claim that the CAC fell, and that it isn't so bad after all, etc., etc. Grand Large is 10% invested in ADLP.

Talk to you again soon,

François

