BANYAN CAPITAL MANAGEMENT

April 25, 2017

Dear Client:

Banyan's equity composite was up 8.6% for the first half of 2017 while the S&P 500 was up 9.3%. While our relative performance for the first half of the year was not as robust as we prefer, we find the nominal results to be satisfactory. (Exclamation of how composite is compiled)

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People regularly compare the stock market to a casino, but that is terribly misguided. Stock prices may fluctuate unpredictably in the near-term, but, over the long-term, business value drives prices. Therefore, investing in the stock market is not an enterprise entirely of chance, although chance is important. It is an enterprise primarily of business valuation and controlling one's emotions.

Leaving the tricky issue of controlling one's emotions aside, let's focus on assessing business value. It is arguably the most important tool in an investor's toolkit, so having a well-developed approach is paramount to success. Conceptually, a business (and any other productive asset) is worth the sum total of all distributable cash flows over the business's life, discounted to the present. That sounds simple. It is not.

In fact, we find the "discounted cash flow" approach unworkable in practice. Few businesses are predictable enough to allow for reliable estimations of distributable cash flows two or three years out, much less ten years out. We could guesstimate, as many do, but that is of little use. At Banyan, we prefer to simplify, which forces us to recognize the imprecision inherent in business valuation.

To do so, we avoid calculating a precise "intrinsic business value" for the businesses we own. Value is in the eye of the beholder, and we recognize that. We focus instead on the "expected return," or "earnings power yield," a business offers at prevailing market prices. We then decide whether that is sufficient given (1) the business's sustainability and (2) our opportunity costs of capital. Simple enough.

Take our investment in Charter Communications ("Charter") as an example. With some conservative adjustments, we estimate that Charter's earnings power yield is roughly 6.6%. At the time of this writing, the most sustainable security on the planet, the 10-Year Treasury, offers a return of less than 2.25% and the earnings yield on the S&P 500 is roughly 5.3%.

The expected return offered by Charter, therefore, is almost 3x that offered by the risk-free proxy (i.e. the 10-Year Treasury) and 25% above that offered by the market proxy (i.e. the

S&P 500). Yet, Charter is a monopolistic business with exceptional management, making its economics far more sustainable than the average business. In other words, Charter is *less* risky than average but boasts an earnings power yield that is *higher* than average.

This alone makes Charter an attractive investment in our opinion. Charter could appreciate 25% and still be undervalued *ignoring growth opportunities*. Yet, the company has clear and meaningful opportunities to grow its earnings power with little incremental capital investment. Therefore, investors are being offered a bargain price for a high-quality asset, and almost certain growth is thrown in for free. What is not to like?

This is how we analyze every investment. To illustrate, we have included below a table showing our earnings power yield calculations for the businesses we own at prevailing market prices. We estimate that our composite businesses offer an average earnings power yield of 6.09%, which is 15% above that offered by the S&P 500 today. (Note that reasonable minds can differ materially on the estimates below.)

Figures in Billions	**Adj. Market Cap**	**Earnings Power (EP)**	**EP Yield**
Wells Fargo	$254.06	$21.20	**8.34%**
Alleghany	$6.99	$0.57	**8.15%**
Apple	$662.98	$51.20	**7.72%**
Amex	$70.50	$5.40	**7.66%**
Post Holdings	$5.44	$0.39	**7.17%**
DaVita	$12.80	$0.90	**7.03%**
Charter	$94.38	$6.21	**6.58%**
Labcorp	$16.02	$1.05	**6.55%**
Berkshire Hathaway	$363.18	$23.00	**6.33%**
C.H. Robinson	$9.24	$0.54	**5.81%**
Sirius XM (LSXMK)	$21.44	$1.22	**5.69%**
Colfax	$5.16	$0.29	**5.66%**
S&P 500	N/A	N/A	**5.30%**
Carmax	$12.11	$0.60	**4.95%**
Fortive	$21.92	$0.96	**4.37%**
Danaher	$57.69	$2.50	**4.33%**
Markel	$11.07	$0.45	**4.09%**
Amazon	$490.24	$15.30	**3.12%**

We also believe our businesses, on average, have far more sustainable economics (i.e. are less risky) than the average business in the S&P 500. Thus, our composite should boast an earnings power yield *below* that offered by the S&P 500. Not to mention most of our businesses have better-than-average potential for profitable growth. Therefore, we believe our composite, as a whole, makes for a very attractive investment.

But make no mistake. There is *nothing* precise about our approach (or any other approach, for that matter). Calculating a business's earnings power yield is a subjective exercise, and assessing risk depends on our understanding of the business and the soundness of our business judgment. That may make some nervous, but, to paraphrase Warren Buffett, we would rather be roughly right than precisely wrong.

Building permanent wealth is our primary goal at Banyan. To do so, we focus first on the preservation of the capital entrusted to us, which depends, in large part, on our ability to assess business value. Only after doing so will we put our clients' hard-earned capital to work.

Sincerely,

Gary L. Watkins
President

Drew D. Estes
Portfolio Manager