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**Nomad Investment Partnership**

**Annual Letter**

**Cumulative returns for the period ended December 31st, 2013**

| To December 31st, 2013: | Nomad Investment Partnership | MSCI World Index (net) US$ |
|---|---|---|
| Trailing: | % | % |
| One year | 62.2 | 26.7 |
| Two years | 126.8 | 46.7 |
| Three years | 104.3 | 38.6 |
| Four years | 194.0 | 54.9 |
| Five years | 404.1 | 101.3 |
| Six years | 176.6 | 19.4 |
| Seven years | 235.3 | 30.2 |
| Eight years | 280.9 | 56.3 |
| Nine years | 316.5 | 71.1 |
| Ten years | 409.8 | 96.3 |
| Eleven years | 815.5 | 161.3 |
| Twelve years | 827.4 | 109.3 |
| Since inception (September 10th, 2001) | 921.1 | 116.9 |
| | | |
| Annualized since inception: | % | % |
| Before performance fees | 20.8 | 6.5 |
| After performance fees | 18.4 | |
| | | |
| Value of a dollar invested at inception (pre-fees) | $10.21 | $2.17 |

The figures above are unaudited, presented on a cumulative, percentage gain basis and, as ever, are before fees. We present results in this way as Nomad's refundable performance fee and time dependent performance fee hurdle mean that the net-of-all- fees results will vary with subscription date, and from investor to investor. Partners will, therefore, each have their own, unique, net-of-all fees experience of investing in Nomad. As a guide, we have also detailed the net-of-all-fees results from one point in time, in this case since inception. An index is used in the table to crudely place our results in context with a broad swathe of share prices from around the world. One of the reasons that Nomad is Nomad is that Zak and I spend almost no time thinking about stock market indices. We do not feel strongly about the merits, or otherwise, of this particular index, indeed its continued inclusion here may have more to do with continuity than relevance, and we would encourage partners to employ another benchmark if they feel it is more helpful to them. Whatever the yardstick, we ask only that Nomad be compared over the very long-term. Below, the same pre-fee results are presented in discrete annual increments. In our opinion, it is probably the upper table that is most useful in assessing long-term investment performance.

| To December 31st: | Nomad Investment Partnership | MSCI World Index (net) US$ |
|---|---|---|
| Calendar Year Results: | % | % |
| 2013 | 62.2 | 26.7 |
| 2012 | 39.8 | 15.8 |
| 2011 | -9.9 | -5.5 |
| 2010 | 43.9 | 11.8 |
| 2009 | 71.5 | 30.0 |
| 2008 | -45.3 | -40.7 |
| 2007 | 21.2 | 9.0 |
| 2006 | 13.6 | 20.1 |
| 2005 | 9.2 | 9.5 |
| 2004 | 22.1 | 14.7 |
| 2003 | 79.6 | 33.1 |
| 2002 | 1.3 | -19.9 |
| 2001 (inception September 10th) | 10.1 | 3.6 |

The annualised return (i.e. before fees) of an investment made in Nomad on September 10th 2001, when Zak and I began managing the Partnership, has been just over twenty percent per annum, as of January 1st this year, whilst the average share, as reflected in the index above, would have seen a return over the same period of around six and a half percent per annum. This fourteen percent or so annual advantage, multiplied out over many years, means that a dollar invested in Nomad all the way through has now grown to be worth just over ten dollars, whilst a dollar invested in the index over the same period would now be worth just over two dollars. Put a slightly different way, and in net asset value terms (i.e. after fees), Nomad has compounded at over eighteen percent per annum, whilst the index has managed an annual six and a half percent.

It appears to all the world that the performance detailed above has been created by Zak and me. That is not the case. In the sense that we could have picked different stocks and performance been poor, then we did avoid a worse outcome. That argument runs in reverse too: performance could always have been better. Even so, in aggregate, the fund management function, evened out over all shareholder experiences, does not add value per se: it only shuffles wealth created elsewhere. As time goes by, the performance that you receive, as partners in Nomad, is the capitalisation of the success of the firms in which we have invested (minus our fees!). To be precise, the wealth you receive as partners came from the relationship our companies' employees (using the company as a conduit) have with their customers. It is this relationship that is the source of aggregate wealth created in capitalism. If you see them at the bar buy a drink for Messrs. Bezos, Robertson, Fernandes, Sinegal, Buffett, Steiner et al, (then call us, that would be quite some bar!). All Zak and I have done is catch some better waves and try to ride them to the shore. Riding waves is not an expensive activity and Nomad's (cost reimbursement) management fee remains around ten basis points per annum.

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This is the twenty-fifth letter to investors over fourteen calendar years. In these letters we have tried to cover the philosophy and methodology Zak and I use to approach the problem of investing. We keep our discussions to as high a level as we can manage in the belief that, in the long run, the high level is all that matters. In these letters we have therefore discussed business models, incentive compensation, capital allocation, mistakes, more mistakes, even more mistakes, lots on psychology and how to think, lots on attitude and so on. Whilst we may only write twice a year, we own shares for such long periods (if the current rate of portfolio activity should persist) that we write around twenty letters during the life of the average investment – that's a huge amount! In previous letters we have also discussed the psychological traps inherent in a more loquacious approach (been there, done that, don't want to do it again!). At its heart, investing is simple, and to make it seem anything but, with the frequent repartition of short-lived facts and data points, may be a conceit. Indeed, it could be argued that a running commentary obfuscates a discussion of the things that really matter. Whilst we have covered many of the topics relevant to long-term investing in these letters already, there is a topic that we have not discussed too much and that now affects the Partnership in a significant way. That is regulation (no moaning at the back).

Since 2001, the number of regulators claiming oversight over the Nomad ecosystem has doubled to four, and the scope of the regulation is up by, we estimate, one order of magnitude. The new Financial Conduct Authority, the fourth iteration of the UK regulator since Zak and I have been in the industry (the others being: the Investment Management Regulatory Organisation, IMRO; the Securities and Futures Authority, SFA; and the Financial Services Authority, FSA), may soon require various parts of the Nomad ecosystem to re-register for authorisation to function as investment service providers. Whilst the process of re-registration can be seen as an expensive form filling exercise, and we are happy to disclose whatever is required (less so about writing the cheques), the nature of the new regulation is unlike its predecessors. Gone is the light touch of self-regulation and instead the mechanism, and perhaps the political will, exists to be far more controlling. For instance, the new regulation seeks a separation of risk management from portfolio management (we are scratching our heads a little on what that means and the regulation does not define the terms) and has already taken the form of mandating remuneration policies (but is oddly silent on dividend payments). As with all new rules there seem to be some anomalies: it appears that an investment advisor in London may be treated as if it is an offshore partnership's general partner for the purpose of regulation, but the same government would view the London entity as a subcontracted investment adviser for the purpose of taxation and control – a contradiction that may not be long lived, especially as governments seek to balance their budgets.

It seems to us that the regulatory landscape is not supportive of small, simple investment boutiques that are not part of whatever problem the regulation seeks to solve. We might wish otherwise, but the halcyon days of the budding stock picker running his friends and family partnership from the sunroom at home at 5505, Farnam Street, Omaha (an image so important to Zak and me) are long gone. In our opinion, given time, the barrier to entry presented by the new rules may cause considerable industry consolidation (a desired outcome from a regulatory standpoint – let's face it, regulation is expensive to do) but consolidation will, in the end, bring with it an unintended, concomitant increase in market fragility, to paraphrase Nassim Taleb. It also seems to us, on an anecdotal basis, that those who increasingly populate the industry are the types who pay others to do their work for them (just witness the Cambrian explosion of service providers offering to act as intermediaries). As some complex financial institutions may be discovering today, if the proprietor has abdicated responsibility to the point of not knowing what is going on, then that is not healthy either.

All this has come about because other people have lied and stolen. In essence we are required to now prove that we are not Bernard Madoff but, unlike Mr. Madoff, there is no potential for us to earn our way to a lighter regime through good behaviour. Nor is any allowance made for the fact that we invest for the very long term or that we are a simple fund. Indeed, Nomad is treated the same as a leveraged, long/short hedge fund complex that deals in exotica and trades constantly. Like traffic speed limits, the regulation seeks to moderate all behaviour for the general good, and we have lived with those restrictions quite happily (well, almost). Even so, in our opinion, what is really required in order to bear down on the liars and cheats are empowered, detectives-cum-regulators asking questions of those whose practices don't sniff right. And if you really want to change industry behaviour, I'll whisper this, tax short term investing. Instead, we get more blanket rules for everyone.

Housekeeping

One of the effects of being closed to subscriptions and only open periodically is that, especially in the current regulatory climate, the Partnership's governing documents can be soon outdated. The investment advisory agreement and prospectus will now be reviewed to reflect (this list is not exhaustive): our status with the SEC; the American FATCA and European AIFMD requirements; our de-listing from the Irish Stock Exchange (which, eh hum, occurred several years ago), and the appointment of Ralph as Nomad's new director following Martin's retirement. That should do it for 2014! The refreshed documents will be sent to partners in due course.

Zimbabwe

In the mid noughties, economic conditions were almost uniformly favourable around the world, and equity market prices reflected the prevailing conditions. In a perfect world, Zimbabwe was a glaring anomaly. In Zimbabwe one could purchase industrial assets, often monopoly or near monopoly operations, for much less than the cost of those assets: cement plants for ten cents on the dollar and breweries for one quarter of the cost of the stills and lorries.

So, we rolled up our sleeves, crossed the border from South Africa, and set about our work. We identified some reasonable investment candidates but the first wrinkle to overcome were exchange controls that artificially over-valued the Zimbabwean dollar. These controls could be legally side stepped through buying shares in firms listed on the Johannesburg (South Africa) stock exchange that also had a listing in Harare (Zimbabwe), re-registering the Jo'berg shares in Harare, and then selling the shares on the Harare stock exchange. The process took some time, but the uplift in purchasing power was many fold above the rate offered by the central bank for cash transactions. With Zimbabwean dollars we could then make investments. We chose three sectors in an attempt to diversify from nationalisation risk, and to invest in businesses with large, powerful, major shareholders who could protect their/our business interests. At least we hoped. To this end we purchased shares in a cement company, brewery and construction/engineering firm.

In the years that followed, the country has lived through: a decline in economic activity of, at one stage, perhaps as much as one half; hyperinflation; the abandonment of the local currency by the central bank as a means of exchange; the suspension of the stock market (and associated zero value attributed to our investments); violent, forced nationalisation of privately owned farms; the attempted assassination of political opponents; and a coalition government which included, and continues to include, the incumbent President Mugabe. Even though Zimbabwe is far from normalised, Nomad's investments have risen in price between three and eight-fold in US dollars and, following the sale of our final Zimbabwean investments last year, the dollars have been remitted to Nomad's bank accounts in London. It is quite a story but, not one we would repeat in a hurry (we can do better with the compounding businesses these days – and they are much less stressful). Enclosed with (the analogue version of) this letter is a one hundred trillion Zimbabwean dollar bank note issued at the peak in hyperinflation (we have a limited number, and so only one note has been enclosed per limited partner. If your letter did not contain a note it is because we may have multiple addressees per limited partner interest, and so the note will be with one of your colleagues). Today the note is worthless (absent an eBay novelty value). But we thought you might like a hundred trillion dollar bill (and who wouldn't?) as a souvenir of Nomad's adventures in capitalism (frame it for the study/boardroom?). (Partners who are more digital in their reading habits may claim their note with an email to Amanda at Galactic HQ – we only have so many, so one application per limited partner, please.)

A final note on Psychology

It is almost ten years since Barry Schwartz published his popular psychology book "The Paradox of Choice". To précis part of the book: Schwartz observed that western society tends to view choice as a good thing, and more choice as better still. In his local supermarket Schwartz counted one hundred and thirty or so different salad dressings, excluding the dozen olive oils and balsamic vinegars should the pre-made salad dressings not offer enough choice! In his local electronics store he found over six million possible combinations of hi-fi components. Even though consumers were being offered what seemed to Schwartz to be an ever-increasing plethora of choice to meet their needs, he could find no correlation with increased happiness. Instead, he hypothesised, that with all the choice came the (subconscious) expectation that the outcome ought to be perfect, and this expectation rendered the actual choice made as disappointing in comparison. It was as if too much choice was making us unhappy.

Schwartz does not make mention of it directly, but the problem is not confined to consumer decision-making. The public stock markets have many tens of thousands of potential investments, and the price of each of those changes almost constantly. The number of possible profit or loss combinations would make Schwartz's hi-fi store look like a multiple-choice test. It is very easy, therefore, to feel unhappy about one's investments. Indeed, on any one day, month, year it is highly likely, indeed statistically almost certain, that one's chosen combination of investments will lag alternatives – there will always be someone who did better.

In a recent Nomad letter (June 2010) we wrote…

"*Readers that make it to the end of our letters (we may be flattering ourselves), including the footnotes (we may be deluding ourselves!), may recall the story we retold of the Ferrari 250 GTO bought by a collector in the 1960s for the effective price of £750. The beauty of* *the story is that although the car is one of the most valuable in the world, the collector still has his car today. A different 250 GTO has recently changed hands, and the price…US$20m!"*

…Stop Press: a Ferrari 250 GTO changed hands recently for U$52m! That represents an annual return of over twenty percent for around fifty years. There is always something going on that makes Nomad's performance look a bit weedy! Before you show your disappointment and reach for the rotten fruit to throw our way, I think it is time we got back to dealing with the regulations (x4).

We wish you a very Happy New Year,

Nicholas Sleep

Our footnotes

There is, we are told, a ticket kiosk at a railway station somewhere in India with a sign above the window that reads, "*No Bamboozlement Here*". It is in the same spirit that we attempt these cautionary words. Disclaimers boil down to the following statement – if you choose to believe any of this, then you are on your own. Yikes! It will be hard for us to escape this conclusion too, and it makes little sense for us to do anything but disclaim liability for errors, omissions and offer no warranties – please, check everything we say, let us know when we are wrong and forgive our errors. We do promise you this: we are human, we make mistakes, but our mistakes are honest ones. Although we do not intend to mislead, we also cannot guarantee the information in these letters, or that some of our ideas may be interpreted in ways we do not intend. As investors we are trying to do as good a job as we can and we write these letters in good faith to inform and educate partners about our actions and thinking in the context of the Partnership. We hope that they will be read in the same spirit in which they are written.

Common sense tells you that the price and value of shares can vary greatly, and whilst we do not aim for this, we also recognize that permanent impairment of capital is possible. Our Partnership is concentrated in relatively few investments, perhaps more concentrated than many others, and as such our results will be more volatile than many of our peers. Nomad is also a very long-term Partnership. We do not think it is suitable for investors with time frames less than five years. We also do not think Nomad is suitable for investors overly conflicted with principal-agent issues. If you are at all uncomfortable then, we suspect, Nomad is not for you.

The Nomad Investment Partnership has had two General Partners: Marathon Asset Management for the period from inception in 2001 to September 2006, and Sleep, Zakaria and Company from September 2006 until the present day. Zak and I have been responsible for the investment decisions of the Partnership since inception, formerly as employees of Marathon and then at our own firm, which was set up for the purpose of managing Nomad. The adventure continues…

Some notes on housekeeping (stay awake at the back!)

This is the annual letter and, combined with the interim letter sent to investors in July, is the main format we use to communicate with our partners. In these letters we have tried to honestly and thoroughly provide all the information we would seek if the tables were turned and we were investors in someone else's fund. We own shares for very long periods and we are conscious that more frequent or detailed reporting may be unnecessary and even counterproductive. A copy of our magnum opus, the full Collection of Letters, is available upon request from Amanda at Galactic HQ (amanda@sleepzakaria.co.uk). Lots of coffee required. Partners in Nomad will also receive a full copy of our Schedule of Investments by separate post, every six months, which lists all of our investments in detail. In addition, in the spring you will receive Nomad's annual accounts, audited by Grant Thornton. Each month statements of account are sent to you by Nomad's administrator (not us!), Phoenix Financial Services in Dublin, Eire. Please call Gavin Gray and his team (+353 18 450 8161) with your statement queries. As should taxable US investors as Gavin and his team prepare their tax certificates (1099s) as well.

Clients should always consider Zak and me to be available at the end of the phone, and our (somewhat shabby) front door open to visitors. And whilst we welcome your company, please don't be too disappointed if we don't have much that is new to say: we hope it is in these letters already.

*Legal footnotes*

*Performance numbers are produced by Phoenix Fund Services, Nomad's administrator, and have been audited by Ernst and Young to 2011, and from then on by Grant Thornton in their annual audits that follow publication of our letters.*

*In our letters we refer to both limited partners in the Partnership, and common shareholders in the Nomad Investment Company (feeder fund) as "partners". We do this to convey a relationship we seek in which our investors are partners in a shared experience and destiny, in which they too have something to contribute. We do not mean to suggest that there is a partnership, in the strict legal sense of the word, between the shareholders in the feeder fund and Nomad, or Sleep, Zakaria and Company, Ltd.*

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*The Nomad Investment Partnership is not a recognized scheme under the Financial Services and Markets Act 2000 ("FSMA"). Given the nature of Nomad's investor base, recourse to the FCA and the Financial Services Compensation Scheme may be limited.*