Roumell Asset Management, LLC

Investment Philosophy

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Roumell Asset Management, LLC ("RAM") pursues long-term capital growth and income through opportunistic value investing. We seek to own a basket of deeply researched, conservatively financed securities that are **out of favor, overlooked, or misunderstood** by Wall Street and thus able to be bought at a significant discount to our calculation of intrinsic value. We believe this strategy maximizes the probability of above-average rates of return over time. Our focus on price is rooted in empirical research which concludes that cheaper than average stocks (low prices relative to earnings, sales, or book value) have historically generated better than average returns over the long run.

RAM is an opportunistic capital allocator. Stocks and bonds are marketed daily like most goods and services in the economy and thus often carry a marketing premium. An opportunistic capital allocator is particularly sensitive to this fact and consequently sits patiently until an investment situation is presented wherein the odds of success are highly favorable, and the reward is multiples of the risk. In the absence of such situations, opportunistic capital allocators, or OCAs, ought to do nothing.

Many believe that investing in simple market exposure will result in adequate returns. We disagree. The financial services industry often references an annualized return of 10% for the period of 1926 to the present. Although that is accurate, it ignores the fact that the S&P 500 (including dividends) failed to produce an annualized return of even 8% in more than 40% of the monthly rolling ten-year periods dating back to 1926. In our opinion, highly price-conscious investors who opportunistically allocate capital are more likely to outperform the market over time.

OCAs have the advantage of waiting for their opportunities, unlike the vast majority of mutual fund managers, who must live with investment mandates to remain fully invested at all times. When will new opportunities arise? The investor never quite knows. Great investing, in our view, is demonstrated in the resolve to relentlessly work, patiently wait, and strike with enough force to have a meaningful portfolio impact.

Our first objective is to be prudent. We are not looking to mirror a particular index; such an approach can readily be found elsewhere. Rather, we are seeking to rigorously exercise our discipline and believe that over time we will generate a meaningful absolute rate of return. Nevertheless, there are drawbacks to opportunistic capital allocation. First, OCAs in general, and deep value-oriented ones like us in particular, can often be quite picky about price and miss reasonable risk/reward investment opportunities while they wait for perfect pitches. Second, if markets rise unabated, we will most likely underperform popular indices—for a period—given our more conservative investment stance and absolute refusal to "chase" securities. During these periods, we are more likely to be net sellers as the price targets of our securities, which are periodically reassessed, are met. It is our belief that the opportunity cost of cash is more than offset by the ability to act boldly when high margin of safety situations are presented. We view our opportunity set as not just what is available today but what may become available tomorrow as well.

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Price versus Value, Plus Patience

Our approach is to seek value wherever we find it, while remaining patient during periods when value is not within reach. We firmly believe that obsessing about price paid has a far greater impact in securing respectable returns than gauging what John Maynard Keynes referred to as "the average opinion of the average opinion." There are multitudes of analysts, commentators, and investors putting forth their opinions about the upcoming direction of gold bullion, U.S. Treasury bonds, and the stock market. We have nothing of substantive value to add to that conversation. We analyze a company as a private business. Thus, for us, while remaining conscious of the overall environment, investing is about price versus value, plus patience, as it pertains to very specific securities purchased at very specific prices.

Although we have a clear bias toward smaller, off-the-beaten-path ideas, we are in fact all-cap investors. Our strategy with regards to larger companies is to search for events in the market, in an industry, or in a particular company that depress security prices below our estimates of intrinsic value. We invest at a time of deep investor disdain and sell these securities when they are simply more rationally priced. The investment edge in these instances lies in a behavioral advantage — that is, the willingness to exercise the greed gene when others are locked in fear.

We believe that our equity investments ought to be augmented by higher-yielding fixed-income investments that provide a steady source of recurring income, to the extent such securities are attractively priced. Although most headlines are dedicated to the stock market's daily activities, we believe that corporate bonds, at times, provide a better risk adjusted return given their senior position in a company's capital structure.

We are not managing for a given quarter or a given year. We manage with a three-year time horizon because the impact of company fundamentals on stocks is diminished over shorter investment periods. To quote Benjamin Graham, "In the short run the market is a voting machine. In the long run it's a weighing machine."

Illiquidity as a Value Proposition

We focus our attention away from the crowd. Often, this approach leads us to invest in smaller companies with more volatile stocks due to modest share counts and lower liquidity. We are not overly concerned about quarterly volatility because we possess something ultimately more important—namely, the conviction in a deep disparity between price and value that we believe will be reconciled in time.

The literature on the value of investing in illiquid smaller securities (e.g., Amihud and Mendelson, 1986; Brennan and Subrahmanyam, 1996; and Pastor and Stambaugh, 2003) was recently updated by the work of Zhiwu Chen, professor of finance at the Yale School of Management, and Roger Ibbotson, professor in the practice of finance at the Yale School of Management and founder of Ibbotson Associates. In *Liquidity as an Investment Style*, published in 2007 and subsequently updated, the two professors conclude, "Going after the most popular stocks does not pay, and investing in illiquidity does." The study's results showed significant return advantage to illiquid securities: from 1972 to 2010, the least liquid quartile of stocks generated an average annual return of 15.62% versus 9.23% for the most liquid quartile. An even starker contrast arises when adding the layer of a valuation component. The least liquid quartile of value stocks generated an average annual return of 20.82% compared to 3.88% for the most liquid quartile of growth stocks.

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We will accept illiquidity in exchange for a discounted price, rather than pay a premium for the privilege of holding liquid, though significantly less discounted, securities. With that in mind, we intend to keep our assets at a size that enables us to remain nimble and participate in less liquid segments of the market that can have a substantial impact on portfolio performance.

We also believe the higher volatility of less liquid stocks can be used to our advantage by averaging down during price declines to reduce our cost basis in specific holdings. Ultimately, our investment success will be determined by our average purchase price, not our initial purchase price.

Investment Edge

Investing is often thought to be a game of numbers focused on valuing assets, future cash flows, profit margins, and the like. While math is essential to investing, it is not sufficient on its own. The question is fair if elusive: what attributes contribute to sustainable, replicable positive risk-adjusted investment results? Our experience as bottom-up, fundamental, deep value investors has taught us to appreciate three critical investment attributes: arithmetic, detective strength, and steady temperament.

Investing is about handicapping probabilities, not about attaining certainty. Math provides the pathway to arrive at reasonable conclusions. First and foremost, companies are dynamic. Many great value investments are purchased at a time of underwhelming earnings. Margins need to be viewed with caution and normalized. Book value is an accounting mechanism that may or may not reflect economic reality. Instead, book value should serve as a starting point to grasp a company's net asset value and needs to be marked up or down to arrive at intrinsic or replacement value. Importantly, net asset value is not synonymous with current earnings power. The analyst must ask: what is the range of outcomes in terms of possible asset sales and earnings power? What discount is needed to provide a sufficient margin of safety given the risks embedded in the story?

"Our research process is relentless and includes regular travel to see management teams, assets, customers, and competitors firsthand."

While math and accounting skills are important, they can only go so far in developing the narrative of an investment opportunity. A large appetite for detective work, in our view, is necessary to gain an investment edge. Roumell Asset Management is at its best when finding small, undiscovered opportunities before investor crowds arrive. Detective work is particularly valuable in getting to the bottom of these undiscovered ideas. At its most elemental level, an investment is a play wherein the investor shows up in the middle act rather than the first. The investment story may be the potential monetization of hidden assets or an increase in future earnings power vis-à-vis market share gains, margin expansion, or secular trends. The analyst needs to ask: what is the nature of the challenge faced by these actors and what are the odds that their methods of engagement will result in a favorable resolution to the specific struggle embedded in this story? In summing up a business's prospects, what do customers, competitors, and others circling the story really think of the enterprise and its leaders? To answer all these questions, we believe you cannot just sit in your office and read about a company and its numbers. Therefore, our research process is relentless and includes regular travel to see management teams, assets, customers, and competitors firsthand.

Interestingly, little has been written about an investor's interviewing skills as a tool for unearthing the truth. The FBI has virtually made a science of the interviewing process with such techniques as first asking a number of questions with known answers to help establish the credibility of the interviewee. For investors like ourselves, once contact has been established with management, an industry source, a competitor, or another player, questions emerge through imagination, creativity and time — all with the goal of getting to the bottom of the story.

Of equal importance to interviewing skills is the analyst's ability to create lasting relationships within various industries. These relationships can provide unique insights and perspectives that can be invaluable in piecing together an investment mosaic. For many years, we have cultivated strong personal contacts that help us in numerous ways: finding new ideas, discussing internally generated ideas, and knowing when to stay away from others.

The third investment attribute that we believe is necessary for successful investing is temperament. Great investors must balance confidence and humility. Here's what often happens in the real world of investing: you've done your valuation/modeling and your detective work, and they both signal a compelling investment opportunity. You purchase the security and then the price falls, sometimes more than you had assumed in your bear case scenario. Now what? Temperament will likely determine your investment outcome because it will mediate the emotional interplay between your math/detective work and the market's current unimpressed view of your investment conclusion. "Did I miss something? Are the sellers better informed than I am? Should I add to my position or sell? Am I selling out of panic or in honest recognition of a mistake?" Anxiety over being wrong can lead to errors of both omission and commission. In this business, you achieve success by managing your emotions as public prices weigh in daily against your calculation of intrinsic value.

We believe our analytical and research strengths are anchored by conservative judgment and mental tough-

ness. Conservative judgment is a temperamental factor that can hardly be overstated. In business, things will go wrong. Management's forecasts sometimes prove too rosy because we all love a good story with a happy ending, but risks never remotely considered will likely emerge. The solution is to demand a healthy margin of safety. Mental toughness is paramount because the ability to remain steadfast in one's analytical conclusions will be tested when dealing with publicly traded securities, given the multitude of short-term factors that contribute to daily pricing.

To wit, investing in public securities occurs within the context of markets composed of human beings wrestling with their own unique emotional histories and personal experiences, resulting in both rational and irrational behavior. Temperament will likely determine whether an investor can effectively leverage his or her math and detective conclusions. In fact, managing during times of extreme market volatility will likely be a key determinant in establishing long-term investment success as measured by the impact of both actual dollar losses and the cost of missed opportunities.

Our portfolio management decisions during the internet bubble and the credit crisis offer two examples of our opportunistic approach and temperamental strength. As the stock market peaked in early 2000, our portfolio had zero exposure to "dot com" stocks because of absurdly expensive valuations and unpredictable business viability. Rather, our portfolio was filled with old economy stocks in which few investors had interest. In the fall of 2008, as the credit crisis was beginning to strangle the markets, our cash balance was 36% of assets, and only 3% of our assets were invested in high-yield corporate bonds. Over the next eighteen months as credit spreads widened dramatically, we invested over 40% of our assets in high-yield corporate bonds across all of our portfolios, while our cash balance declined by nearly 40%. In both instances, cash helped protect us as panic gripped the markets, and cash also enabled us to take advantage of bargains created by the panic.[1]

Specific Security Selection versus Market Exposure

Why are we not fully invested at all times? In a word: pricing. We are not in the business of handicapping Fed actions, liquidity flows, or other events driving overall market momentum, or the direction of select asset classes. We are in the business of valuing companies (in terms of their earnings power and asset value), determining an appropriate discount level required to live with the risks embedded in the security, and buying when that price level is met. We ask this central question: would we take this company private in a heartbeat? One doesn't take a company private as a result of anticipated Fed action, interest rate expectations, or attempts to handicap money flows into select asset classes. That's market "stuff," and it's not what we do.

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We take comfort in our portfolio of conservatively financed companies with unique assets which we own at meaningful discounts to our calculation of intrinsic value. We invest predominantly in companies with strong balance sheets, an approach that we believe dramatically reduces our risk of permanent loss of capital. The companies in which we invest possess valuable assets, tend to have substantial cash positions, and are typically unencumbered by significant liabilities. We believe selecting specific securities at very specific prices will prove to be the most effective way to manage risk while capturing attractive rates of return over time.

We are focused on sourcing exceptional value but-

[1] Please refer to our Annual Disclosure Presentations. Roumell Asset Management, LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented those reports in compliance with the GIPS standards. Roumell Asset Management, LLC has been independently verified by Ashland Partners & Company LLP.

tressed by original research, a willingness to think independently, and the temperament to see the process to fruition. Our portfolio concentration can result in higher volatility. We do not view volatility as commensurate with risk because volatility is different than permanent impairment of capital. While volatility can be distressing, it creates exceptional investment opportunities for those poised to exploit it. We are willing to leverage our deep value discipline to concentrate on our best ideas; we typically hold between 25 and 35 securities, compared to well over 100 securities for the average mutual fund.

However, we do make mistakes in selecting securities. In 2007, for instance, we purchased a basket of poorly performing businesses, albeit well-capitalized ones, that we believed were take-out candidates. When private-equity financing dried up we were stuck with these businesses and our performance for the year was negative versus a positive year for the general market. In 2011, our individual security holdings diverged from the market and we again experienced a period of negative returns when the overall market advanced. We put a high focus on extracting lessons from our mistakes.

"Our belief in the crucial role of incentives is reinforced by our own practice of investing right alongside our clients."

In Search of Good People

In selecting investments, we ask ourselves: do we want to partner with this management team? Do we think they are honest? Do we believe they are good operators and smart capital allocators? We are not looking for perfection, but we are seeking to go into business with people of integrity who work hard and who are properly incentivized. Sizing up management is a critical component of our investment process.

We disagree with the view that management teams aren't worth talking to because their answers are often suspect. We believe it is well worth our time to talk to managers, to visit with them, to observe their decision making over time, and to interview their colleagues and competitors to the extent possible. We are looking to develop a management narrative that must begin with asking basic questions. Who is the CEO as a person, and what is her or his reputation? What is the company's culture? Does management turn over regularly? Answering each of these questions helps us develop a picture of the people involved in the operations underlying our investment positions.

The Greek philosopher Heraclitus said simply, "Character is destiny." Plato's dialogues are discussions about how to live — conduct — one's life. When asked about the lasting lessons of Enron, William Powers, the lead investigator into the firm's collapse, and now president of the University of Texas, said, "You need to surround yourself with good people who are competent, honest — and are not going to take shortcuts." In selecting investments, we are actively looking for managers with talent and integrity. Unfortunately, some on Wall Street and in the halls of corporate America never absorbed basic ideas of fairness and stewardship. Rather than risking their own capital, they too often are hired hands who are given incentives to place outsized bets with the hope of inflating their own compensation. Our belief in the crucial role of incentives is reinforced by our own practice of investing right alongside our clients.

The heart of American business is found on Main Street. Firms across the country have done much to warrant pride. Our focus is on smaller enterprises, which are often below Wall Street's radar, where management is often "all in" with both their hearts and pocketbooks. We are constantly in pursuit of well-capitalized companies managed by hardworking, dedicated leaders who possess vision, take their stewardship responsibilities seriously, and understand their obligation to shareholders. However, we're only interested in investing in these companies when we believe they are on sale.

Roumell Asset Management, LLC

Core Tenets

1. We find value by pursuing securities that are out of favor, overlooked, or misunderstood, where an analytical, informational, or behavioral edge is more likely as compared to popular securities, which are well understood by most investors.

2. We analyze a company as a private business. The price we pay for a common stock must be at a substantial discount to what we believe the issuer is worth as a private company. We ask ourselves if we would want to own the entire company at the price being offered.

3. In the absence of compelling investment opportunities, we hold cash.

4. We invest predominantly in companies with strong balance sheets, an approach that we believe dramatically reduces our risk of permanent loss of capital. The companies in which we invest possess valuable assets, tend to have substantial cash positions, and are typically unencumbered by significant liabilities.

5. We do not share the common view that volatility is risk. While volatility can be distressing, it creates exceptional investment opportunities for those poised to exploit it. Further, it offers us the chance to reduce the average cost on our existing positions. We simply believe thorough research and a great price ultimately trump the discomfort of volatility.

6. Because our investments are based on specific knowledge, we have less of a need to over-diversify. We typically invest about 5% of our portfolio in each of our highest-conviction ideas, whereas most mutual funds often invest only 2% in high-conviction ideas. We believe that our best ideas deserve much more of our capital.

7. Management teams with whom we partner are measured by integrity, drive, competence as operators and capital allocators, and incentives to do right by shareholders.

8. We invest in corporate bonds, most often supported by hard assets, that offer attractive yields and are protected by rights to claim assets ahead of common and preferred stock.

9. Our research process is relentless and includes regular travel to see management teams, assets, customers, and competitors firsthand.

10. We measure ourselves on a rolling three-year basis because the gap between market value and intrinsic value often does not close in one quarter or even one year.

11. Our price targets are periodically reassessed to account for any events that may impact intrinsic value. When our price targets are met, we sell.

12. We believe that the temperament to remain steadfast in our analytical conviction, especially when others are consumed by fear or blinded by enthusiasm, is necessary to obtaining superior long-term returns. Further, flexibility must be maintained in order to avoid the pitfalls of overconfidence.

Pictured above from left to right: Ted Crawford, Jim Roumell, Craig Lukin, Jason Mackey, and Sherita Morris.

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