ZPR Investment Report

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A NEWSLETTER FOR ZPR CLIENTS

US Commentary

By Mark Zavanelli

US stock averages were mixed in April, but small caps generally did better and our US strategies had an excellent month. We have seen before that when your style and process is working it can overcome a difficult market. We have also seen our share of frustrating periods of underperformance as we are now seeing in Asia. Small cap value has been out of favor for a long time in the US and elsewhere, and if the tide is turning there is plenty of catching up to do. Valuation gaps have gotten very wide as investors have paid up for both safety (think Utilities) and growth (think Internet or Biotech). Just looking at the table that Vaidas and Giedrius put together this month you can see the difference in pricing between a value strategy and the S&P 500. While safety and growth both sound nice, at the wrong price they actually make for bad investments. We're encouraged by the performance of a couple of our quant strategies, Volume Value and Volume Winners, which are the antithesis of the hot stocks since they look for companies with little investor interest.

The big news in the market since the bottom in February continues to be the "reflation" trade. This has seen commodities, including oil, rally along with riskier assets while the dollar has

(Continued on page 4)

Asian Results

By Vaidas Petrauskas

While our U.S. stocks shined in April, our Asian stocks were struggling. As far as the performance of the broad markets, the Japanese Nikkei 225 index closed down 0.55% for the month, the Singapore FTSE ST All Share index closed down 0.10%, and the Thai SET index was down 0.22%. We estimate our holdings lagged the indices in all three markets in April. All three Asian currencies gained against the U.S. dollar with the Yen gaining almost 5%. The Yen gained 3% on only the last trading day of the month after the Bank of Japan failed to announce new stimulus measures, which the market fully expected them to do.

Our Japanese holdings have been especially disappointing this year. I will give you one example. We started buying one of our largest current holdings in Japan in June 2010 at 318 yen. Their earnings have more than doubled since then and the stock has been a winner. It rose past 1000 yen in 2013 and traded sideways until 2015 where it doubled to over 2200 yen in July (this is not meant to characterize our performance as we also have many Japanese stocks which performed poorly and have produced losses). It was still cheap at 2200 yen, otherwise we would have reduced our position. It is now at 1008 yen, and many of our accounts have a loss since purchasing it. What happened since July of last year? The company reported two great quarters with earnings growing at 72% in the third quarter of 2015 and 35% in the 4th quarter. At 1008 yen the stock

(Continued on page 3)

May Contents:

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Portfolio Statistics and Stock Selection

By Vaidas Petrauskas and Giedrius Rupeika

We would like to share with you the calculations that we recently performed showing the valuation, growth, and other ratio averages of our holdings by country. We think the table below will be useful for our investors to understand why we invest in the markets that we do, and to have a better understanding of what kind of stocks we hold. All data is as of April 28th close.

We usually look for stocks that have at least 100% upside according to the model. This gives us a big enough margin of safety if we are wrong. GRAPES favors highly profitable (high Return on Equity) companies and this is reflected in our holdings. The stocks in Japan are so cheap, selling at less than book value, that GRAPES almost takes a back seat.

	ZPR Holdings in:				
	Thailand	Singapore	Japan	U.S.	S & P 500
Price/Earnings TTM	7.5	8.7	7.7	12.3	23.8
Price/Book Value	1.5	0.6	0.9	1.5	2.9
Return on Equity (Median)	19.6%	7.5%	12.4%	14.3%	15.3%
Net Income Growth – LFY (Median)	31.5%	-19.9%	18.1%	21.4%	1.7%
GRAPES upside (Median)	102.0%	95.0%	159.0%	102.0%	7.0%
Market Cap (USD) Mill. (Average)	$340	$783	$205	$1,119	$38,373
Dividend Yield (Average)	5.6%	6.2%	2.5%	1.0%	2.0%

The first thing to note is that the U.S. stock market, represented by the S&P 500 index, is more or less fairly valued according to the GRAPES theory. U.S. corporate earnings barely grew in the last fiscal year (1.7% growth for the median S&P 500 company). But our holdings are much cheaper with much better growth and upside according to GRAPES. This includes the impact of a higher cost of capital in Asia (6% vs. 4% in the US). Also, the average dividend yield of our Thai and Singaporean companies is especially impressive.

The profits of our Singaporean companies shrank by almost 20% last year and the stock prices followed. Unfortunately, in Singapore our greatest value stocks have been either oil or shipping related with a few exceptions. So these have suffered and the stocks now are too cheap to sell. Singapore still remains the free port of the world and all goods from Europe, Australia, and most of the rest of the world must pass through Singapore, making it one of the wealthiest countries in the world.

You can see why we invest in Japan. 18% growth with 12% ROE selling at 90% of book value. But last year's growth is history. The Japanese economy has stalled and we have shifted some capital from Japan to Thailand.

We also want to share with you our approach for looking for new stocks.

The way we look for new stocks is similar across all the markets. Our GRAPES Theory of stock prices plays a major role in both the screening for new stocks and in making trading decisions.

For U.S. companies, ZPR has a proprietary ICX3000 quarterly database which we build ourselves and which starts with the first quarter of 1986. At the end of each quarter we add the data for the largest 3000 U.S. companies to the database. The database is our primary research tool and also the backbone of our quant strategies. We screen for Asian securities using the Thomson Reuters database. We look for undervalued stocks first and foremost but we do not blindly buy any cheap stock. We typically wouldn't buy a stock of a company with an expected decline in earnings due to cyclical or secular reasons. We look for growth. Our approach is similar to the GARP (Growth at a Reasonable Price) strategy introduced by Peter Lynch. We wouldn't buy a loss-making business unless we think a turnaround is imminent. We never buy heavily indebted companies because the preservation of capital is our primary goal. Avoiding losers is no less important than finding winners.

Once the screening is done, the hard work of fundamental analysis is performed. We read the 10-K, 10-Q, proxy statement for insider deals, listen to conference calls. We buy stocks of companies that we believe will increase earnings and intrinsic value over time. We seek long-term growth drivers. These are usually country, sector or company specific e.g. low rubber price benefiting companies that use rubber in production, government incentives benefiting real estate developers. When we think we have found a stock with a good risk-reward profile we usually take a small position and increase it over time as we get more familiar with the story and the company keeps performing well.

Asian Results (Continued)

is trading at net current asset value and 4.4 P/E! So, yes, investing in Japan can be disappointing but we are able to find great bargains and as long as companies keep growing their intrinsic value, the stock prices will have to catch up eventually. While some of our own holdings have disappointed and were sold, there are plenty of cheap stocks and we have added new holdings. One of the main reasons for the recent drop in the Japanese stock market is the selling of foreign investors. Macro players are very active here and cause short term distortions. Not only are they selling but also shorting Japanese equities. The short selling ratio rose to unprecedented levels recently. The ratio was 20% in 2012. Now it is at 40%. The determined plan of Prime Minister Shinzo Abe to raise the VAT once again from 8% (it was 5% a year ago) to 10% next year isn't helping the stock market either. The rise in VAT will hurt consumption and profit margins. Abe is not backing down from this terrible decision. There is no attempt at all to cut government spending, which is the real problem. Instead of cutting their bloated government and spending, the Japanese government is raising taxes. Many failed stimulus programs and debt at 229% of GDP - far worse than Greece. Japanese save more of their earnings than anyone else. All those deficits were financed directly by the Japanese savers' money, otherwise they would have runaway inflation. Now no matter how hard they try, they can't even get 1% inflation or any sustainable economic growth. The Japanese currency continues to appreciate making egg on face for the Bank of Japan. The rest of the world considers it a safe haven. If stocks weren't ridiculously cheap in Japan, with many stocks selling at or below net current assets, we wouldn't be there.

Meanwhile, we are happy to see that our Thai stocks are doing well this year, even though they were down slightly in April. The junta is still in power and not going away anytime soon. But they appointed great people to run the country's finances. Realizing they know nothing about economics, they brought in Somkid Jatusripitak, a free markets and pro-business economist, as deputy prime minister. The junta is clever. They prevent assembly, but allow freedom of the press and leave the journalists alone. The academics are called in and detained until they recant if they speak badly of the junta. The new constitution that the junta is drafting is a mockery that keeps the military in power for 6 years. The draft of the constitution that was announced allows the military junta a five year "transitional period" before full civilian rule is restored. That's five years from the next general election which will not be before the summer of 2017. Neither the King nor the majority of Thai people seem to object. It is about stability. The unemployment rate is 1%. So people are happy. Stability and great economics are great for investing. Thailand, the real Asian tiger, is back.

US Commentary (Continued)

fallen. Mostly this is the pendulum swinging back the other way from the “sky is falling” trade of the prior months. We’ve commented in the past about the power of speculators to link these things in the market while the economic correlation is something less. In reality the sky isn’t falling and we’re also not off to the races in terms of faster growth. China still has to get past its current financial mess and will not be the marginal demand driver that it was. In the US unfortunately we are no longer set up for fast growth, and if we try too hard it will only result in inflation. But the consumer is in good shape and that means the economic cycle will continue to plod along. Slow is actually ok. Maybe growth does reaccelerate in the second half, although if it brings inflation we’ll wish it hadn’t. Despite all the hand wringing this is really just continuation. During this expansion rough periods for stocks have been followed by better periods, and I don’t see why that won’t be the case this time. Going forward I think there are plenty of opportunities for returns in the US since value stocks are cheap, but there will also be volatility to go along with that.

The key change from my perspective is that the long trend of the dollar rising and commodities falling seems to be at the least flattening out here. This is something that we predicted at the beginning of the year and that has major implications. While that trend was occurring we saw continuous flows of money out of international markets and into the US, causing the US market to outperform by a large margin and keeping bond yields low. Well, trees don’t grow to the sky and trends don’t last forever. Now those flows are likely to taper off and the relative performance is likely to shift too. This could be a long trend, since foreign markets are cheap both relative to the US and in absolute terms.

Just the Numbers

	Period Ending 4/30/16			Period Ending 3/31/16				
ZPR Composites Names in Bold *Benchmarks in italics*	Month	Quarter To Date	YTD	1 Year	3 Year Annualized	5 Year Annualized	Inception (if < 5 yrs)	Incep. Date
ZPR Fundamental Small Cap Value	5.76%	5.76%	9.48%	-4.55%	11.75%	8.59%		
Volume Winners	3.61%	3.61%	4.60%	14.40%	13.92%	10.04%		
Volume Value	5.95%	5.95%	4.85%	6.41%	14.87%	15.06%		
Volume Momentum	1.33%	1.33%	-2.44%	-9.21%	6.64%	10.08%		
Russell 2000	1.51%	1.51%	-0.03%	-9.76%	6.84%	7.20%		
S&P 500	0.27%	0.27%	1.62%	1.79%	11.83%	11.58%		
ZPR Global Equity	1.62%	1.62%	0.07%	-9.37%	1.73%	7.18%		
MSCI ACWI	1.54%	1.54%	1.93%	-3.80%	6.10%	5.80%		
ZPR All Asian	-1.08%	-1.08%	-6.27%	-10.87%	-3.61%	6.97%		
MSCI EAFE	3.00%	3.00%	0.04%	-7.87%	2.67%	2.79%		
ZPR All Thai Equity	-0.35%	-0.35%	9.14%	-3.48%	-0.80%		16.81%	1/1/12
Thai Set Index	-0.22%	-0.22%	10.13%	-3.51%	-0.18%		11.53%	1/1/12

Composite returns are presented net of management fees and trading expenses, and include the reinvestment of dividends and other income. All returns are in US dollars except for the Thai Set Index, which is presented in Thai Baht.

Past performance does not guarantee future results. The table above reflects (1) performance of the ZPR Investment Management, Inc. ("ZPR"), composites named in bold in the first column, (2) performance of the benchmark which reflects the composite's investment mandate, objective, or strategy, and (3) performance of the S&P 500 Index, which is provided for overall comparison and informational purposes. Please see the reverse for important information about composite and benchmark descriptions, how to receive more complete information about the composites, and disclosures regarding the calculation of performance, among other matters. Subsequent markets may perform better or worse than for the periods shown, which will cause the actual results of a portfolio to be better or worse than shown. ZPR does not guarantee or offer any assurance that any portfolio or account will be profitable, meet a client's stated objectives, or prevent or reduce losses. **A client may lose money by investing in a portfolio.**

ZPR Investment Management, Inc. ("ZPR") is an SEC registered investment adviser managing separate accounts that are fully discretionary. SEC registration does not constitute an endorsement of the firm by the Commission nor does it indicate that the adviser has attained a particular level of skill or ability. ZPR claims compliance with the Global Investment Performance Standards (GIPS™). To receive a complete description of the policies and procedures for any composite, a list and description of all ZPR composites, and a presentation that complies with the GIPS standards, please contact us at 386-775-1177 or zprim@mpinet.net.

All composites include fully discretionary, management fee-paying and, beginning on January 1, 2011, non-management fee-paying accounts, including those accounts no longer with the firm. The U.S. Dollar is the currency used to express performance, except for the ZPR All Thai Equity Strategy, for which performance is expressed in the Thai Baht. Returns are presented net of management fees and include all trading expenses and the reinvestment of all income. Net of fee performance was calculated using actual management fees, except in the case of non-fee paying accounts where model fees have been imputed. Actual advisory fees and transaction fees will vary depending on, among other things, the portfolio, account size, and activity. Fees are described in ZPR's ADV Part 2A.

The benchmark and other data provided was obtained from publicly available reports, including internally derived databases and other resources available to ZPR. ZPR believes such data to be reliable but does not audit, verify, or guarantee its accuracy or completeness. When comparing the performance results to a benchmark, clients should keep in mind that: 1) Indexes are unmanaged and unavailable for direct investment. 2) Benchmark returns include reinvestment of income, but do not reflect taxes, or investment advisory or other fees that would reduce performance. 3) Performance information of benchmark indexes is included for comparison purposes only.

Composite and Benchmark Descriptions:

The S&P 500 and Russell 2000 are market cap weighted indices of large company and small company US stocks, respectively.

The Fundamental Small Cap Value Composite consists of accounts that hold U.S. small cap stocks selected by using ZPR Fundamental Analysis. This analysis identifies undervalued companies using ZPR's GRAPES valuation model and also applies other selection criteria relating to a company's business prospects, management quality, and capital structure. The benchmark for the composite is the Russell 2000 Index, presented in U.S. Dollars. In the past the composite has displayed higher volatility than its benchmark.

The Volume Winners Composite consists of accounts that hold U.S. micro cap stocks selected by using ZPR Volume Winners Analysis. This analysis is a quantitative evaluation system incorporating volume, momentum and valuation measures. The benchmark for the composite is the Russell 2000 Index, presented in U.S. Dollars. In the past the composite has displayed lower sensitivity to market returns than its benchmark, which would cause it to underperform in a strongly rising market.

The Volume Value Composite consists of accounts that hold U.S. micro cap stocks selected by using ZPR Volume Value Analysis. This analysis is a quantitative evaluation system incorporating volume and valuation measures. The benchmark for the composite is the Russell 2000 Index, presented in U.S. Dollars.

The Volume Momentum Composite consists of accounts that hold U.S. micro cap stocks selected by using ZPR Volume Momentum Analysis. This analysis combines two quantitative evaluation techniques; ZPR's price and earnings momentum measure SuperMo, and ZPR's volume, momentum and value system Volume Winners. The benchmark for the composite is the Russell 2000 Index presented in U.S. Dollars.

The Global Equity Composite consists of accounts that hold both U.S. and International stocks selected by using ZPR Fundamental Analysis. This analysis identifies undervalued companies using ZPR's GRAPES valuation model and also applies other selection criteria relating to a company's business prospects, management quality, and capital structure. The benchmark for the composite is the MSCI All Country World (Gross) Index, presented in US Dollars. MSCI ACWI is a market capitalization weighted index comprised of equities from developed and emerging markets, including the US. The composite has historically held small cap stocks from a limited set of countries while the benchmark weighting is primarily composed of larger companies spread across many countries. This is likely to cause the composite to have greater volatility than its benchmark. The composite includes the performance of accounts that may occasionally use margin; however, the use of margin is not part of the overall strategy of the composite.

ZPR All Asian Composite consists of accounts that hold Asian stocks selected by using ZPR Fundamental Analysis. This analysis identifies undervalued companies using ZPR's GRAPES valuation model and also applies other selection criteria relating to a company's business prospects, management quality, and capital structure. The benchmark for the composite is the MSCI EAFE Index, which is comprised of equities from developed markets around the world, excluding the US and Canada. MSCI EAFE is presented in U.S. Dollars. The composite has historically held small cap stocks from a limited set of countries, including emerging markets, while the benchmark weighting is primarily composed of larger companies from developed countries. This is likely to cause the composite to have greater sensitivity to the returns of countries where it invests, and overall greater volatility than its benchmark.

The ZPR All Thai Equity Strategy consists of accounts that hold Thai stocks selected using ZPR's Fundamental Analysis. This analysis identifies undervalued companies using ZPR's GRAPES valuation model and also applies other selection criteria relating to a company's business prospects, management quality, and capital structure. The benchmark for the composite is the Thai Set (TRI) Index, a market capitalization weighted index of securities listed on the Stock Exchange of Thailand and presented in Thai Baht. The composite has historically held small cap stocks while the benchmark weighting is primarily composed of large companies. This is likely to cause the composite to have greater volatility than its benchmark.