Dear Shareholders:

Overview

FPA Crescent returned 2.95% in the second quarter and 10.38% in the first six months of 2013, as compared to the S&P 500's returns of 2.91% and 13.82% respectively.

The second quarter's winners and losers are as follows:

2013 Q2 Winners & Losers

Winners	Losers
Microsoft	Covidien
Cisco	Canadian Natural Resources
Omnicare	Tesco

The largest three contributors added 1.28% to our second quarter return, while the detractors cost the fund 0.53%. In the past, we have described our investments in Canadian Natural Resources and Tesco, and while the price of each has bounced around, other than that little has changed. Covidien had the biggest positive impact on Q1's performance, only to decline so much in Q2 that it topped the "Losers'" chart. While still early in the quarter, Q2's "Winner", Microsoft, is now trying to pull a "Covidien" as it is leading the early Q3 charge for poor performance. Needless to say, stock prices change far more than intrinsic value and our quarterly reporting of winners and losers only serves to answer the frequent question as to what drove the Fund's recent performance. We suggest you don't read any more into it than that, as it is more a curiosity than a foreteller of future performance.

Ultimately, we pay more attention to the underlying financial performance of the companies in our investment portfolio than we do their stock charts and in one instance, Omnicare, the largest supplier of pharmaceuticals to patients in nursing homes, delivered in spades. New management came in several years ago and began executing on a business plan that revolved around basic blocking and tackling to improve performance. While the engineer of the turnaround, John Figueroa, has handed off the plan to his successor, the momentum remained intact under the present CEO, John Workman. The company has lowered costs, reduced customer churn, won new accounts and essentially built the best mousetrap in the institutional pharmacy space. The net result is that all of the aforementioned improvements in aggregate have manifested themselves in the form of higher and more consistent earnings. Those achievements and the belief that the company's future continues to look bright are reflected in a stock price that has more than doubled from our original cost.

Economy

Our views on the economy are not terribly original and have not changed significantly in the past six months. It's a challenge finding new ways to say the same thing. So we won't. We think our past commentaries effectively communicate our longstanding view that as we exited the 2008-9 financial crisis, the average Joe on the street was left with less in his bank account, a diminished home value, and what stocks he did own weren't worth as much. When Joe could afford less, the U.S. government stepped in and spent in his place, and hasn't stopped spending since. What the Joes of the world can't afford, the U.S. government apparently can – but don't ask us to explain that "new" math. The recovery has been disappointing and largely

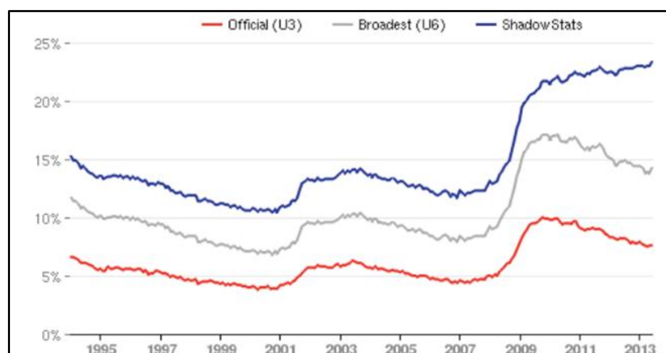
engineered by central bank policy. We worry that low interest rates and novel and theoretical Fed policy could lead to unintended consequences.

The past quarter included a brief hiccup when investors considered their exposure to low interest rates in the event the Fed allows rates to normalize. There was a lot of discussion in the media during the past quarter regarding how and when Ben Bernanke intends to taper the purchase of bonds by the Federal Reserve. Interestingly, we can't recall having a single conversation internally about the taper, as this simply isn't how we look at the world. We are worried about how a business and the world might look three to five years from now, not next quarter. In fact, if one thinks back five years, the world has dealt with a great financial crisis, potential currency collapse and fears of sovereign liquidity, just to name some of what we have seen. Through it all, we invested with a long-term strategy dependent on patience, discipline and a focus on long-term value. With an average holding period of roughly five years, we strive to add value over a full business cycle rather than try to guess where central bankers may move interest rates

On the other hand, many investors who took a myopic approach and chased short-term yields were met with a rude surprise this past quarter as interest rates spiked higher. During this period, rate sensitive investments – including real estate investment trusts (REITs) - declined in value, especially those that use leverage to invest in leases. Our appreciation for the macro backdrop, coupled with our value standards, has resulted in the portfolio eschewing yield enhancing investments (REIT, MLP, Bonds) over the past few years.

The apparent decline in the unemployment rate is something of a bright spot in the US economy, but as you know, we have long held reservations about how this statistic is reported. Unemployment has largely declined because many have left the workforce.[1] Since 1984, on average, 66% of the population worked, but now it's just 64%.[2] That may not seem like much of a change, but for every 1% of the population that gives up seeking work, unemployment declines by 1.5%. If one were to assume that the U.S. shouldn't be any different than it has been historically, then unemployment would currently be 10.6%. In addition, the ranks of the employed include an increasing number of people working part-time, but many part-time workers would prefer full-time employment.[3] John Williams' Shadow Government Statistics tries to get to the truth behind government economic reporting. His less sanguine view of unemployment is represented below and reflects a new record high. We don't know if his number is correct but we certainly agree directionally, as does Mr. Bernanke, who said that the current unemployment rate is "not exactly representative of the state of the labor market."

Unemployment Rate Official (U-3 & U-6) vs. ShadowStats Alternate
Monthly S.A. Through June 2013



Source: ShadowStats.com. Published July 5, 2013.

---

[1] Bureau of Labor Statistics, bls.gov. June 2013 not seasonally adjusted.

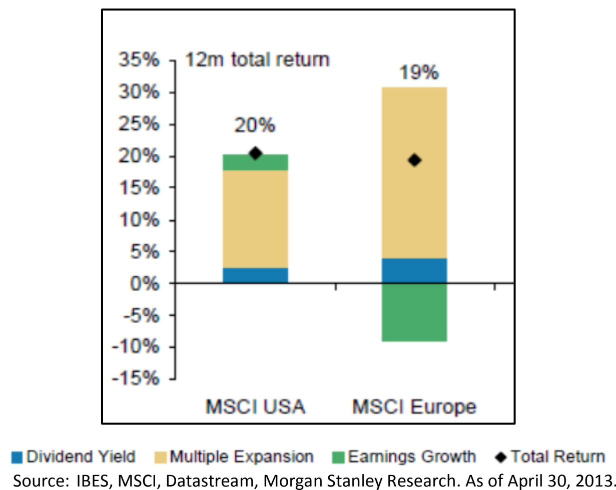
[2] Population = civilian non-institutional population, excluding, among other people, those younger than 16 years and those who have been incarcerated.

[3] Unemployment is going down due, in some immeasurable part, to Obamacare. The Patient Protection and Affordable Care Act (PPACA) requires that beginning in 2015, companies must provide health insurance to those employees who work 30 hours a week or more. Many companies are reducing payroll hours ahead of time, particularly those that already operate with a significant portion of part-time labor (like restaurant chains) with the commensurate benefit being an increase in employment, albeit part-time. The unforeseen side effect of the PPACA is many employers are reducing weekly hours below the 30 hour/week threshold that requires that they provide healthcare to employees.

We would like to believe that Fed officials understand this, but you wouldn't know it from the way they talk. In their June 19 press release, Fed officials said, "the Committee reaffirmed its expectation that the current exceptionally low range for the funds rate will be appropriate at least as long as the unemployment rate remains above 6½ percent so long as inflation and inflation expectations remain *well behaved*." We have already established that the unemployment rate definition is loose at best, but now we apparently have to determine the nature of inflation's comportment. Instilling little confidence, the Fed interprets this combination of data and tea leaves to justify its bond purchasing taper and ultimate exit. The Fed governors seem to be using, as the Scot poet Andrew Lang once wrote, "statistics as a drunken man uses lamp posts, for support rather than illumination."

Government assistance has yet to be felt in any kind of substantive, let alone sustainable, way. But the Fed, along with other central banks, has certainly been successful in lifting asset prices. As can be seen below, the vast majority of the market's return in the U.S. and Europe over the past year has been driven by multiple expansion.

Multiple Expansion Still the Predominant Driver of Returns



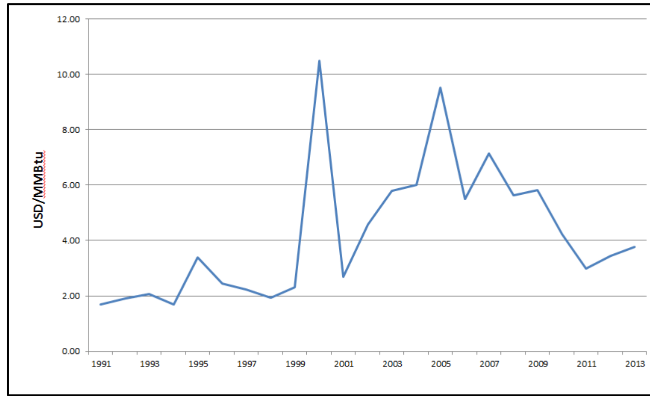
Dividend Yield Multiple Expansion Earnings Growth ◆ Total Return

Source: IBES, MSCI, Datastream, Morgan Stanley Research. As of April 30, 2013.

We find it difficult to invest in an environment that seems manipulated to engineer higher asset prices regardless of business fundamentals. So, instead, we allow cash to build and spend our time building an actionable inventory for the future.

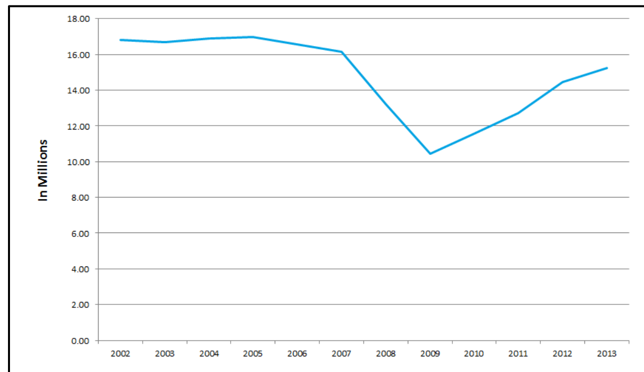
Despite our fiscal policy concerns, we recognize that economies have a way of overcoming difficulties and that there are a number of bright spots in the US. In particular, housing looks to be entering a period of strength. U.S. manufacturing continues to have the benefit of lower input costs, thanks to natural gas prices that remain far lower than in many parts of the industrialized world. What's more, auto sales are still well below average and the construction industry (commercial and residential) is still far off its peak.

U.S. Natural Gas Prices



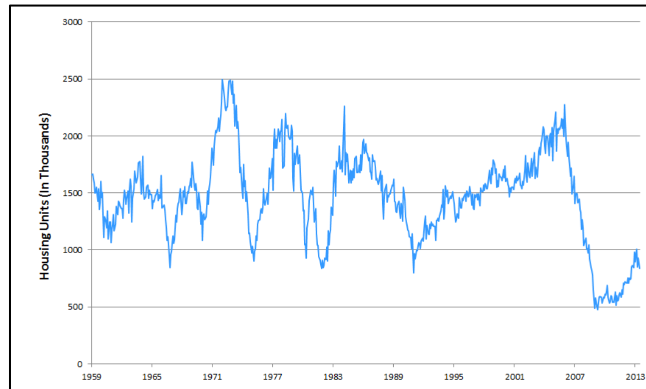
Source: Bloomberg energy, as of June 11, 2013.

U.S. Auto Sales



Source: ACEA,OICA, and regional motor associations, as of May 31, 2013.

U.S. Housing Starts



Source: St. Louis Federal Reserve . Data as of June 1, 2013.

If this brief discussion leaves you wanting and frustrated, then we have succeeded in fostering a feeling that sits in the pits of our stomachs. We wish we could offer more, but we are torn between a concern over the unintended consequences of novel policy and the knowledge that things tend to work out in the long run. As

for the portfolio, we invest when we find opportunities that offer a margin of safety[4] and the prospect of an attractive real return. We avoid those investments that appear overly exposed to obvious macro excess. Macro excess can go on for years, though, so as we discuss in the following Investments section, we continually investigate a broad swath of prospective investments – companies, industries, asset classes, all located in different geographies, mostly public but some private.

Investments

That said, an upward sloping chart is not the optimal environment for us to deploy capital, particularly when equities aren't cheap, except in relation to bonds. Although bearish on bonds, we are neither bullish nor bearish on stocks but reflectively cautious.

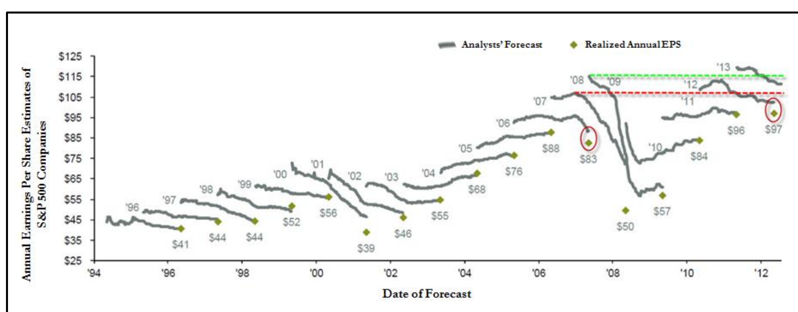
We continue to research our companies in the same disciplined fashion. When companies become attractive in our conservative base case earnings scenarios, we will make an investment even against what might be an ugly macro-economic backdrop. We believe a good business at a great price always demands the commitment of capital and invariably trumps whatever larger fears may be impacting that company, its industry or the general economy.

We begin our process by looking for those good companies that are operating below their potential, or ones for which there are concerns that the good times won't last. There may be valid reasons that justify why a company is out of favor, but we work to establish that it is either ephemeral or already accounted for in the price.

The vast majority of the time we strive to gain a deep, holistic understanding of a business. Occasionally, however, an investment might resemble more of a statistical businessman's wager. By deep understanding, we mean that in addition to studying the financial statements and footnotes, we also try to understand the capabilities of the management team, which can admittedly be more touchy-feely. A by-product of this work is our earnings and cash flow models, which we use to frame risk and reward.

We do not try and determine what a company can earn in a particular quarter or year because we appreciate the limitations of our work. Wall Street thinks differently and offers tremendous precision as to what a company may earn each quarter. Unfortunately, that's a fool's errand. As you can see in the chart below, in the vast majority of years, the optimism of Wall Street analysts' gets the better of them, with earnings estimates typically being consistently reduced from the beginning of the year through the four seasons.

Wall Street Optimism



Sources: FactSet, J.P. Morgan Asset Management. Data are as of 3-14-13. S&P 500 Annual Earnings Per Share Estimates, operating basis, weekly consensus estimates, annual reported EPS.

We choose, instead, to develop a model that includes a low and high case, but we place more emphasis on a conservative base case EPS[5] looking out 3-4 years. We then place conservative valuation multiples (e.g. P/E[6]) on each case to determine a target price. We aren't smart enough to try and place probabilities on each of the cases, but we are generally inclined to invest when the base case suggests we will make a respectable return,

---

[4] Buying with a "margin of safety" is when a security is purchased for less than its estimated value. This helps protect against permanent capital loss in the case of an unexpected event or analytical mistake. A purchase made with a margin of safety does not guarantee the security will not decline in price.

[5]EPS (Earnings per share) is the portion of a company's profit allocated to each outstanding share of common stock.

[6]Price/Earnings ratio (P/E) is the price of a stock divided by its earnings per share.

while the high case suggests we will do better still, and the low case suggests we may not lose money during our expected holding period. Looking back, we've historically done a respectable job of steering clear of landmines. On the flipside, we have made more than our share of errors of omission due to our conservatism, a trade-off we are happy to live with, particularly in the current environment.

Three technology companies that we own serve as an example of our process. Microsoft, Oracle and Cisco have seen their share of media bashing and not without good reason. However, we believe that the negative sentiment created an opportunity for us to arbitrage the difference between perception and reality. Here are some headlines from the past year:

If it wasn't for bad news, they'd have none at all

These three companies all face real challenges, including poor management and/or competition from new technologies. But we feel, in each case, the prices adequately discount those fears.

While it can be dangerous looking in the rear view mirror when investing in technology, we believe it is important to point out that while the growth of the three companies in question has slowed from their respective peaks, the group as a whole continues to grow faster than most companies in the S&P 500.

MSFT, ORCL, CSCO Continue to Grow Faster than the Market

	Revenue Growth 2002-2012	Revenue Growth 2007-2012	EPS Growth 2002-2012	EPS Growth 2007-2012
MSFT, ORCL, CSCO Average	10%	10%	15%	13%
S&P 500 Median	7%	5%	13%	9%

Source: Capital IQ. As of April 30, 2013.

So all else equal, we prefer companies with strong balance sheets and this group has those. Moreover, even though cash is akin to a lead weight that depresses a company's return on capital calculation, these companies offer a much higher return on capital than the S&P 500.

MSFT,ORCL, CSCO Return on Equity (ROE)

	ROE 2002-2012	ROE 2012
MSFT, ORCL, CSCO Average	27%	22%
S&P 500 Median	14%	15%

Source: Capital IQ. As of April 30, 2013.

Consistent with our portfolio approach to seek out companies that offer non-US exposure, the three tech companies in question all have global businesses in the truest sense of the world, generating almost half their

sales from outside of the US. This is not unique to the portfolio, as we have made a concerted effort to gain exposure to markets outside of the United States. In fact, at the portfolio level, Crescent currently has 48.3% of its sales sourced outside North America, with that figure driven by both international holdings and domestic holdings with foreign revenue.

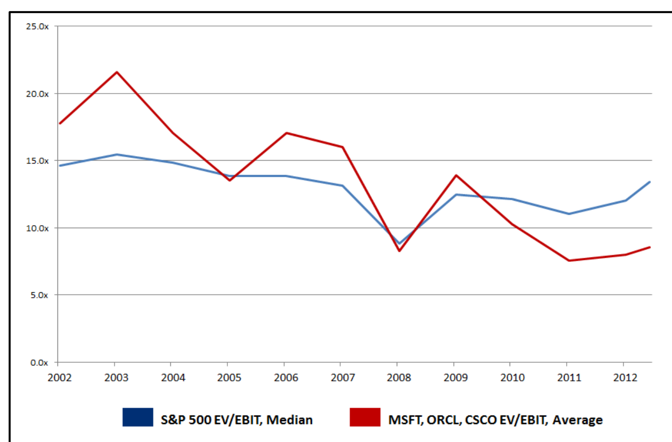
Revenue Composition of Equities in FPA Crescent

Region	Revenue Exposure
North America	51.6%
South America	2.5%
Uncategorized Americas	2.7%
Western/Northern Europe	15.5%
Eastern Europe	0.8%
Asia/Pacific	8.5%
Middle East/Africa	2.0%
Uncategorized Non-U.S.	16.3%

Source: Bloomberg

Our three tech musketeers now trade less expensively than they have versus the S&P 500 median on a historical basis as measured by either EV/EBIT[7] or P/E[8].

EV/EBIT ~ S&P 500 vs. MSFT, ORCL and CSCO

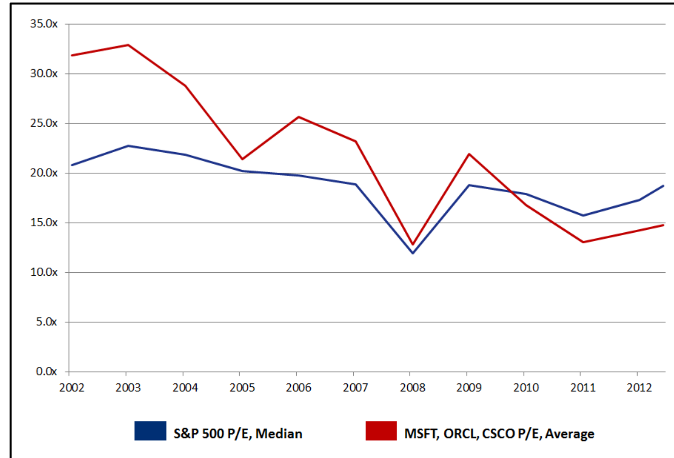


Source: Capital IQ. As of April 30, 2013.

[7] Enterprise Value is a measure of a company's value, often used as an alternative to straightforward market capitalization. Enterprise value is calculated as market cap plus debt, minority interest and preferred shares, minus total cash and cash equivalents. EBIT or earnings before interest and taxes is an indicator of a company's profitability, calculated as revenue minus expenses, excluding tax and interest.

[8] Price/Earnings ratio (P/E) is the price of a stock divided by its earnings per share.

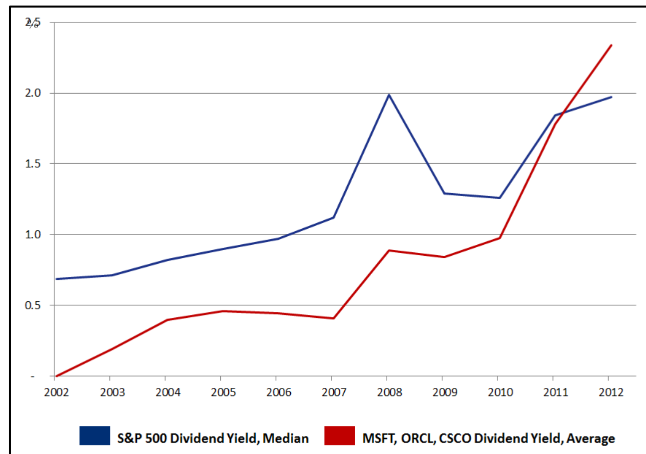
P/E ~ S&P 500 vs. MSFT, ORCL and CSCO



Source: Capital IQ. As of April 30, 2013.

These companies had not historically offered a dividend yield, but now with cash flow exceeding internal investment opportunities, they each now pay a dividend and offer yields in excess of the market.

Dividend Yield ~ S&P 500 vs. MSFT, ORCL and CSCO



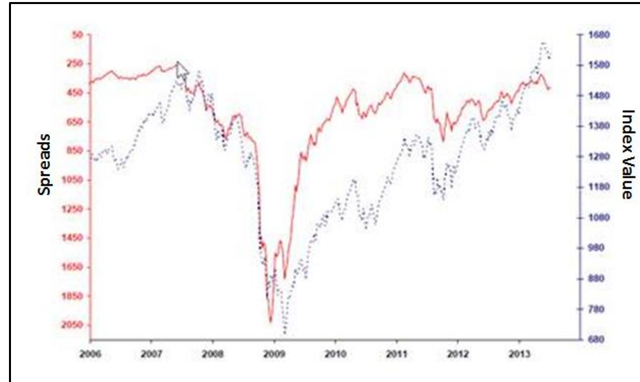
Source: Capital IQ. As of April 30, 2013.

Given our purchase price and conservative target multiples, we are optimistic about the return potential for each of these companies. We reemphasize that our earnings (and revenue) estimates are less than that of Wall Street. We consider "owner earnings" when establishing our base case, rather than GAAP (General Accepted Accounting Principles) earnings. We, therefore, reduce net income by cash used for stock options and further ding earnings for "required" M&A (Mergers & Acquisitions) that we view as imperative to remain relevant and to sustain earnings on a going forward basis.

We believe that our Contrarian Team's bottoms-up process of analyzing Microsoft, Oracle and Cisco is replicable. Returns may be transient, but process is not. This is the only way that we know how to manage money. We've done it this way for more than two decades and commit to you that this will not change. We can't tell you what the world will look like tomorrow or when Bernanke will raise rates, but we will borrow a line from the investment strategist, Dylan Grice, who said it best when he quipped, "I'm interested in the possibility of building a profitable portfolio which is robust to my ignorance."

High Yield / Distressed

S&P 500 (--) vs. Junk Spreads (inverted scale)



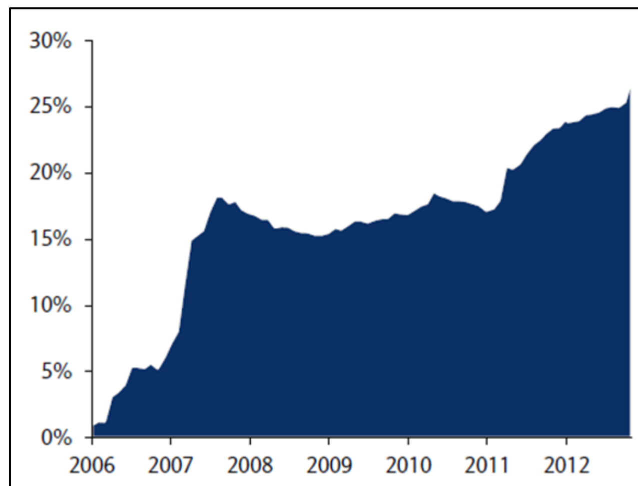
Source: Macro Mavens

High Yield New Issuance

		Ba	B	Caa	NR	Total	Caa +NR %	$Caa +NR $	Redeem %
Yearly	1996	23,928	40,819	1,336	6,471	**72,554**	10.8%	7,807	19.9%
	1997	44,406	71,814	6,091	9,433	**131,744**	11.8%	15,524	24.2%
	1998	38,570	72,787	12,309	13,638	**137,304**	18.9%	25,947	19.0%
	1999	26,648	60,217	1,875	2,544	**91,284**	4.8%	4,419	47.9%
	2000	12,784	23,655	3,205	4,717	**44,361**	17.9%	7,922	74.9%
	2001	31,492	45,800	1,543	813	**79,648**	3.0%	2,356	46.3%
	2002	17,421	39,435	1,435	255	**58,545**	2.9%	1,690	58.5%
	2003	33,323	87,712	7,446	1,831	**130,313**	7.1%	9,278	45.7%
	2004	34,468	78,100	21,291	543	**134,403**	16.2%	21,835	64.0%
	2005	25,142	54,698	13,213	410	**93,462**	14.6%	13,623	62.4%
	2006	50,113	70,927	19,821	1,508	**142,368**	15.0%	21,329	50.8%
	2007	27,607	75,862	33,136	1,763	**138,368**	25.2%	34,899	68.6%
	2008	13,263	25,142	10,214	1,121	**49,739**	22.8%	11,335	114.5%
	2009	49,731	87,345	14,063	1,461	**152,599**	10.2%	15,524	68.8%
	2010	63,933	151,102	43,409	4,210	**262,654**	18.1%	47,619	51.2%
	2011	74,007	116,552	33,617	4,080	**228,256**	16.5%	37,707	66.0%
	2012	91,480	188,868	54,408	9,809	**344,566**	18.6%	64,217	52.2%
	2013	36,445	72,164	28,227	4,812	**171,083**	19.3%	33,039	36.5%

Source: Barclays Capital. As of May 31, 2013. Unit of measure is in billions. Ba, B, Caa signify Moody's ratings.

Covenant Lite Levered Loans as % of Issuance



Source: Barclays Capital. As of November 30, 2012.

Need we say more?

Conclusion

Whether good environment or bad, our focus is to consistently balance the natural tension that accompanies both protecting your capital and preserving your purchasing power. We can't promise to do either over the short-term, but if you are willing to commit to us over a full business cycle, we think our team has a fighting chance to accomplish these goals.

Along these lines, in case you did not see the announcement last month, I warmly welcome Brian Selmo and Mark Landecker to join me as Portfolio Managers of the Fund. As discussed in the press release celebrating the Fund's 20 year anniversary, the three of us comprise the Contrarian Strategy investment committee and have been effectively serving as Portfolio Managers for the FPA Crescent Fund for the last couple of years. Now Brian and Mark have the title to go with the role.

Since we manage Crescent as if you have entrusted all of your money to us – although we don't recommend it – we persistently seek to maintain the appropriate balance of reward and risk. Thank you for your continued trust.

Respectfully submitted,

Steven Romick
President
July 20, 2013