



# SOURCE CAPITAL, INC.

**FIRST QUARTER REPORT**

March 31, 2019

# SOURCE CAPITAL, INC.

## LETTER TO SHAREHOLDERS

### DEAR SHAREHOLDERS:

#### Performance

During the first quarter of 2019, the net asset value per share return of Source Capital, Inc. (or the “Fund”) was 10.23%, and 11.36% on a market price basis (both percentages including the reinvestment of the distributions paid during the period). These changes compare with a 13.65% return for the S&P 500 Index, a 2.94% return for the Bloomberg Barclays U.S. Aggregate Bond Index and a 9.31% return for the 60/40 blended S&P 500/ Bloomberg Barclays U.S. Aggregate benchmark during the same period.<sup>1</sup>

The Fund’s top five winners and losers for the first quarter of 2019 are presented below. The winners contributed 2.74%, while the losers detracted -0.04%.<sup>2</sup>

<u>Winners</u>	<u>Performance Contribution</u>	<u>Losers</u>	<u>Performance Contribution</u>
Altaba	0.62%	Petroleum Helicopters Int.	-0.02%
Analog Devices	0.56%	Fortress Credit Opp. 10.3% 2028	-0.01%
Alphabet	0.53%	GNMA 0.8% 2053	-0.01%
United Technologies	0.52%	GNMA 0.8% 2053	-0.01%
Broadcom	0.51%	Pacific Gas & Electric	0.00%

The stock market delivered the best quarterly return in a decade, and the best quarterly start to a year since 1998.<sup>3</sup> It’s almost as if the drawdown in the preceding fourth quarter didn’t happen with the S&P 500 and MSCI ACWI indices increasing 13.65% and 12.18% in the first quarter, respectively.

<sup>1</sup> Comparison to the S&P 500 Index and the Bloomberg Barclays U.S. Aggregate Index is for illustrative purposes only. The Fund does not include outperformance of any index or benchmark in its investment objectives.

<sup>2</sup> Reflects the top contributors and top detractors to the Company’s net asset value performance based on contribution to return for the quarter. Contribution is presented gross of investment management fees, transactions costs, and Fund operating expenses, which if included, would reduce the returns presented. The weights of the winners and losers within the portfolio as of March 31, 2019 were: Altaba (2.7%), Analog Devices (2.8%), Alphabet (4.4%), Jardine United Technologies (0.6%), Broadcom (3.2%), Petroleum Helicopters Int. (0.0%), Fortress Credit Opportunities 2016 7I E. 10.3% 2018 (0.1%), GNMA 0.8% 2053 (0.1%), GNMA 0.8% 2053 (0.2%), Pacific Gas & Electric (0.0%). The information provided does not reflect all positions purchased, sold or recommended by FPA during the quarter or year-to-date. A copy of the methodology used and a list of every holding’s contribution to the overall Fund’s performance during the quarter and year-to-date is available by contacting FPA Client Service at [crm@fpa.com](mailto:crm@fpa.com). It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities listed. **Past performance is no guarantee, nor is it indicative, of future results.**

<sup>3</sup> ‘Stock market’ refers to the S&P 500 Index. Third quarter 2009 S&P 500 Index return was 15.61%. First quarter 1998 S&P 500 Index return was 13.95%.

On the fixed income side, treasury yields declined during the quarter and the treasury yield curve inverted. Specifically, the metric that many market observers watch – the difference between the 2-year treasury and the 10-year treasury – stayed positive throughout the quarter. However, the metric that has been a better predictor of recessions – the difference between the 3-month treasury and the 10-year treasury – inverted briefly before reversing. Meanwhile, credit spreads in both investment grade and high-yield bonds decreased meaningfully. Together, lower rates and lower spreads led to lower market yields.

### **Open Market Repurchases**

We started the quarter with the market discount to net asset value of 13.55% and ended the quarter with the discount at 12.77%. We repurchased 40,329 shares in the first quarter of 2019 at an average discount of 12.60%. The shares repurchased were accretive to shareholders by adding \$0.02 per share to the Fund's NAV.

As a reminder, Source Capital is authorized to make open-market repurchases of its common stock of up to 10% of the Fund's outstanding shares at such times as its shares trade at a greater than 10% discount to the Fund's net asset value, when in FPA's judgment such repurchases would benefit shareholders, subject to various factors, including the limitations imposed by the federal securities laws governing the repurchase of an issuer's stock by the issuer and the managers' ability to raise cash to repurchase shares in a tax-efficient manner. There is no assurance that Source Capital will purchase shares at any specific discount levels or in any specific amounts.

Respectfully submitted,

Source Capital Portfolio Management Team  
April 2019

## Important Disclosures

On December 1, 2015, a new portfolio management team assumed management of the Fund and the Fund transitioned to a balanced strategy. Performance prior to December 1, 2015 reflects the performance of the prior portfolio manager and investment strategy and is not indicative of performance for any subsequent periods.

*Current performance information is updated monthly and is available by calling 1-800-982-4372. Performance data quoted represents past performance, which is no guarantee of future results. Current performance may vary from the performance quoted. The returns shown for Source Capital are calculated at net asset value per share, including reinvestment of all distributions. Returns do not reflect the deduction of taxes that a shareholder would pay on Fund distributions, which would lower these figures. Since Source Capital is a closed-end investment company and its shares are bought and sold on the New York Stock Exchange, your performance may also vary based upon the market price of the common stock.*

*The Fund is managed according to its investment strategy which may differ significantly in terms of security holdings, industry weightings, and asset allocation from those of any indices noted herein. Overall Fund performance, characteristics and volatility may differ from the benchmark(s) shown.*

*There is no guarantee the Fund's investment objectives will be achieved. You should consider the Fund's investment objectives, risks, and charges and expenses carefully before you invest. You can obtain additional information by visiting the website at [www.fpa.com](http://www.fpa.com), by email at [crm@fpa.com](mailto:crm@fpa.com), toll free by calling 1-800-279-1241 (option 1), or by contacting the Fund in writing.*

The views expressed herein and any forward-looking statements are as of the date of this publication and are those of the portfolio management team. Future events or results may vary significantly from those expressed and are subject to change at any time in response to changing circumstances and industry developments. This information and data has been prepared from sources believed reliable, but the accuracy and completeness of the information cannot be guaranteed and is not a complete summary or statement of all available data.

Portfolio composition will change due to ongoing management of the Fund. References to individual securities are for informational purposes only and should not be construed as recommendations by the Fund, the Adviser, the portfolio managers, or the distributor. It should not be assumed that future investments will be profitable or will equal the performance of the security examples discussed. Please visit our website, [www.sourcecapitalinc.com](http://www.sourcecapitalinc.com), for a complete list of portfolio holdings.

Investing in closed-end funds involves risk, including loss of principal. Closed-end fund shares may frequently trade at a discount or premium to their net asset value.

Investments, including investments in open-end or closed-end mutual funds, carry risks and investors may lose principal value. Capital markets are volatile and can decline significantly in response to adverse issuer, political, regulatory, market, or economic developments. It is important to remember that there are risks inherent in any investment and there is no assurance that any investment or asset class will provide positive performance over time. Small and mid-cap stocks involve greater risks and may fluctuate in price more than larger company stocks. Short-selling involves increased risks and transaction costs. You risk paying more for a security than you received from its sale.

The Fund may purchase foreign securities, including American Depositary Receipts (ADRs) and other depository receipts, which are subject to interest rate, currency exchange rate, economic and political risks; these risks may be heightened when investing in emerging markets. Foreign investments, especially those of companies in emerging markets, can be riskier, less liquid, harder to value, and more volatile than investments in the United States. Adverse political and

economic developments or changes in the value of foreign currency can make it more difficult for the Fund to value the securities. Differences in tax and accounting standards, difficulties in obtaining information about foreign companies, restrictions on receiving investment proceeds from a foreign country, confiscatory foreign tax laws, and potential difficulties in enforcing contractual obligations, can all add to the risk and volatility of foreign investments.

Fixed income securities are subject to interest rate, inflation and credit risks. The return of principal in a fund that invests in fixed income securities is not guaranteed. Lower rated bonds, convertible securities and other types of debt obligations involve greater risks than higher rated bonds. Interest rate risk is when interest rates go up, the value of fixed income securities, such as bonds, typically go down and investors may lose principal value. Credit risk is the risk of loss of principle due to the issuer's failure to repay a loan. Generally, the lower the quality rating of a security, the greater the risk that the issuer will fail to pay interest fully and return principal in a timely manner. If an issuer defaults, the security may lose some or all its value.

Mortgage securities, asset-backed securities, and collateralized mortgage obligations (CMOs) are subject to prepayment risk and the risk of default on the underlying mortgages or other assets; such derivatives may increase volatility. Convertible securities are generally not investment grade and are subject to greater credit risk than higher-rated investments. High yield securities can be volatile and subject to much higher instances of default. The Fund may experience increased costs, losses and delays in liquidating underlying securities should the seller of a repurchase agreement declare bankruptcy or default.

Value style investing presents the risk that the holdings or securities may never reach their full market value because the market fails to recognize what the portfolio management team considers the true business value or because the portfolio management team has misjudged those values. In addition, value style investing may fall out of favor and underperform growth or other styles of investing during given periods.

#### Index Definitions

Comparison to any index is for illustrative purposes only and should not be relied upon as a fully accurate measure of comparison. The Fund will be less diversified than the indices noted herein, and may hold non-index securities or securities that are not comparable to those contained in an index. Indices will hold positions that are not within the Fund's investment strategy. Indices are unmanaged and do not reflect any commissions or fees which would be incurred by an investor purchasing the underlying securities. An investor cannot invest directly in an index. The Fund does not include outperformance of any index or benchmark in its investment objectives.

**S&P 500 Index** includes a representative sample of 500 leading companies in leading industries of the U.S. economy. The index focuses on the large-cap segment of the market, with over 80% coverage of U.S. equities, but is also considered a proxy for the total market.

The **Bloomberg Barclays U.S. Aggregate Bond Index** provides a measure of the performance of the U.S. investment grade bonds market, which includes investment grade U.S. Government bonds, investment grade corporate bonds, mortgage pass-through securities and asset-backed securities that are publicly offered for sale in the United States. The securities in the Index must have at least 1-year remaining in maturity. In addition, the securities must be denominated in U.S. dollars and must be fixed rate, nonconvertible, and taxable.

**60% S&P 500/40% Bloomberg Barclays Aggregate Index** is a hypothetical combination of unmanaged indices comprised of 60% S&P 500 Index and 40% Bloomberg Barclays U.S. Aggregate Bond Index, representing the Fund's neutral mix of 60% stocks and 40% bonds.

#### Other Definitions

**Yield to Worst** is the lowest potential yield that can be received on a bond without the issuer actually defaulting.

**SOURCE CAPITAL, INC.**  
**TOP TEN HOLDINGS**

March 31, 2019  
(Unaudited)

	<u>Percentage of Net Assets</u>
American International Group, Inc. ....	3.58%
Broadcom, Inc. ....	3.17%
Arconic, Inc. ....	2.78%
United Technologies Corp. ....	2.77%
Analog Devices, Inc. ....	2.77%
Altaba, Inc. ....	2.68%
Comcast Corp. (Class A) ....	2.60%
Citigroup, Inc. ....	2.50%
Bank of America Corp. ....	2.37%
Baidu, Inc. (ADR) (China) ....	<u>2.28%</u>
Total	<u><u>27.50%</u></u>

# SOURCE CAPITAL, INC. PORTFOLIO SUMMARY

March 31, 2019  
(Unaudited)

<b>Common Stocks</b> .....		<b>60.0%</b>
Internet Media .....	9.9%	
Diversified Banks .....	6.1%	
Semiconductor Devices .....	5.9%	
Aircraft & Parts .....	5.5%	
Cable & Satellite .....	4.8%	
Cement & Aggregates .....	3.8%	
P&C Insurance .....	3.6%	
Electrical Components .....	2.1%	
Investment Companies .....	2.1%	
Infrastructure Software .....	2.1%	
Midstream – Oil & Gas .....	1.9%	
Banks .....	1.7%	
Insurance Brokers .....	1.7%	
Generic Pharmaceuticals .....	1.6%	
E-Commerce Discretionary .....	1.5%	
Mining Services .....	1.5%	
Consumer Finance .....	1.5%	
Home Improvement .....	1.2%	
Application Software .....	0.7%	
Food & Drug Stores .....	0.6%	
Base Metals .....	0.2%	
<b>Closed End Fund</b> .....		<b>2.7%</b>
<b>Bonds &amp; Debentures</b> .....		<b>32.8%</b>
Asset-Backed Securities .....	16.0%	
Residential Mortgage-Backed Securities .....	9.3%	
Commercial Mortgage-Backed Securities .....	3.8%	
U.S. Treasuries .....	1.6%	
Corporate Bank Debt .....	1.1%	
Corporate Bonds & Notes .....	1.0%	
<b>Short-term Investments</b> .....		<b>4.4%</b>
<b>Other Assets And Liabilities, Net</b> .....		<b>0.1%</b>
<b>Net Assets</b> .....		<b><u><u>100.0%</u></u></b>

**SOURCE CAPITAL, INC.**  
**COMPOSITION OF NET ASSETS\***

March 31, 2019

Investment securities (cost \$309,694,508):	
Common stocks .....	\$210,641,370
Bonds, debentures and other investments .....	115,243,766
Closed End Fund .....	9,399,899
	<u>\$335,285,035</u>
Cash, receivables, short-term corporate notes, less liabilities .....	15,626,099
Net assets at March 31, 2019 .....	<u>\$350,911,134</u>

**SUMMARY FINANCIAL INFORMATION\***

	Three Months Ended March 31, 2019	
	Total Net Assets	Per Common Share
Beginning of Year .....	<u>\$321,869,963</u>	<u>\$37.66</u>
Net gain on investments, realized and unrealized .....	\$ 31,486,056	\$ 3.69
Net investment income .....	1,103,707	0.13
Distributions to Common shareholders .....	(2,129,902)	(0.25)
Cost of Capital Stock repurchased .....	(1,418,690)	0.02
Net changes during period .....	<u>\$ 29,041,171</u>	<u>\$ 3.59</u>
End of period .....	<u>\$350,911,134</u>	<u>\$41.25</u>
	Beginning of Quarter	End of Quarter
Common market price per share .....	\$32.55	\$36.00
Common net asset value .....	\$37.66	\$41.25
Common market discount from net asset value .....	13.57%	12.73%

\* The financial information included in this report has been taken from the records of the Fund without examination by independent auditors. Securities are carried at fair value.



# SOURCE CAPITAL, INC.



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Alfred E. Osborne, Jr.  
A. Robert Pisano  
Patrick B. Purcell

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Mark Landecker, *Portfolio Manager*  
Brian Selmo, *Portfolio Manager*  
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Abhijeet Patwardhan, *Portfolio Manager*  
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## **STOCK EXCHANGE LISTING**

New York Stock Exchange: SOR