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THIRD POINT

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Fourth Quarter 2014 Investor Letter

Review and Outlook

Since the financial crisis, managing volatility and risk has proven to be almost as important as good stock-picking in generating investment returns. Last year emphasized this lesson, as investors struggled to cope with five drawdowns of greater than 3.9% in the SPX followed by swift rebounds within weeks. Third Point's mediocre 2014 results, +5.7% in Offshore and +6.8% in Ultra, were due to a combination of poor trading during market volatility and bad judgment in exiting positions for reasons ranging from "overstaying our welcome" to impatience seeing our thesis through in choppy markets. Fortunately, there were bright spots in structured finance and enough winners in equity and government credit to help us eke out a mid-single digit return for our investors.

Already, 2015 has been marked by increasing volatility, prompting a banker friend (hat tip to Jimmy L.) to characterize this as a "haunted house market" where a new scary event lurks around each corner. Out of this year's 25 trading days, 22 have had intra-day moves in the market of more than 1%.

Haunted house scares so far this year have included: 1) signs of lower growth across the globe despite falling oil prices; 2) the depegging of the Swiss Franc, which caused an overnight 15% move; 3) declining currencies from Japan to Europe putting pressure on US companies' earnings and competitive position; 4) a disconnect between when the Fed expects to raise rates and what the market is forecasting; 5) the rise of populism and the anti-austerity left in Europe which has underscored how fragile the "union" of this fragmented continent is today; 6) Russian incursions into the Ukraine; 7) chaos in the Middle East; 8) a surprising lack of leadership on the international stage by the United States and an apparent unwillingness to take decisive action to promote democracy abroad; and 9) a seeming decline in government respect for rule of law, shown by numerous executive actions, confiscations of property, and use of various departments — ranging from the IRS to the Treasury — to intimidate citizens and interfere with legal commerce.

In this environment, we are investing in companies with solid cash flow and consistent growth. The markets remain favorable for constructive engagement with management teams to improve capital allocation, streamline operations, and drive shareholder value, particularly in large cap companies which have not had to engage with shareholders in the past. We are looking to add exposure during market dislocations. After a lackluster year for credit in 2014, we are starting to see value in energy-related names and potential opportunities to reload our portfolio.

We have also lowered our gross and net exposures this year. Despite recognizing that volatility had increased last year, in hindsight, our net exposures remained too high for too long due to conviction in our long stock picks and a small short book. This portfolio posturing meant that, for the first time since 2008, we were harmed rather than helped by the market's five significant drawdowns, missing out on the chance to purchase securities cheaply during periods of panic. These missed opportunities undermined mostly successful stock picking and uniformly favorable resolutions of our constructivist campaigns.

While we obviously believe our top positions will be worth more in the long run, we expect a fair amount of volatility in the interim. Avoiding dramatic downside in individual names and sizeable losses during inevitable sell-offs will be key to succeeding in this market and navigating successfully through the haunted hallways of 2015.

Quarterly Results

Set forth below are our results through December 31st and for the year 2014:

	Third Point Offshore Fund Ltd.	S&P 500
2014 Fourth Quarter Performance*	-0.3%	4.9%
2014 Year-to-Date Performance*	5.7%	13.7%
Annualized Return Since Inception**	17.3%	7.7%

*Through December 31, 2014. ** Return from inception, December 1996 for TP Offshore Fund Ltd. and S&P 500.

Select Portfolio Positions

Equity Position: Amgen

Our biggest winner in 2014 was our equity position in the biotechnology company Amgen. In our last letter and at the Robin Hood Investment Conference, we highlighted Amgen as a hidden value situation where investor skepticism in three areas – R&D productivity, operating efficiency, and capital allocation – had obscured the company's fundamental value.

From our perspective, Amgen's valuation discount to both biotech peers and even slower-growing pharmaceuticals was unwarranted given Amgen's compelling mix of longduration, highly cash-generative mature assets and soon-to-launch blockbuster products. To create shareholder value, we made three specific recommendations: 1) focus the company's R&D efforts; 2) provide long-term margin guidance demonstrating a commitment to reducing a bloated cost structure; and 3) create clarity on additional shareholder returns.

Apparently, Amgen Chairman and CEO Bob Bradway recognized many of the same sources of investor frustration and he has responded with a company-wide transformation initiative. At Amgen's Analyst Day in October, Mr. Bradway directly addressed two areas of shareholder skepticism: operating margins and capital allocation. The company shared long-term operating margin and cost reduction targets with investors, noting that 2018 spending will not exceed 2013 levels. This expense discipline should help drive operating margins from 38% to at least 52% over that period. In addition, Amgen guided to a 30% increase in its quarterly dividend and accelerated the resumption of its share repurchase program. The long-term vision and discipline presented at the Analyst Day combined with several subsequent positive clinical pipeline events helped Amgen return nearly 45% to shareholders in 2014, the best performance of all mega cap US healthcare companies and Amgen's highest annual return since 1999.

Even so, we feel this story is still in its early innings and there is still substantially more value for Amgen shareholders to realize. We believe the company can be more aggressive with its share repurchase program, particularly since the stock remains undervalued at current levels. We also remain focused on Amgen's R&D productivity, given the company's disappointing returns on its $30 billion in R&D spending over the past decade. While changes to R&D can take longer to implement, we expect that Mr. Bradway will remain attentive to this area. We hope that the company's recent immuno-oncology partnership with Kite Pharmaceuticals exemplifies Amgen's increasing efforts to broaden its R&D capabilities in a financially responsible way. Our work suggests further meaningful opportunities exist to improve and optimize internal processes, particularly around decision-making and project selection. Finally, we believe Amgen should provide more granular detail (e.g., R&D spending by therapeutic area) to investors to provide comfort that its current R&D decisions reflect a careful approach to managing capital.

We look forward to continuing to work with the company and our distinguished Third Point Scientific and Medical Advisory Board Members – Dr. David Agus, Dr. Geoff Ginsburg, and Dr. David Parkinson – to further help tune up a world-class engine of scientific discovery and innovation.

Equity Position: FANUC

During the fourth quarter we invested in Fanuc (the "Company"), the leading factory automation and robotics company in the world with a market capitalization of $33 billion and an enterprise value of $25 billion. Based in Japan and spun out of Fujitsu in the 1970's, Fanuc is a unique company with a long history of being the best and fastest to market in everything it does. Its visionary founder describes the Company's mission as "walking the narrow path," which refers to its relentless focus on producing only a limited number of products that are technically superior with the lowest possible cost structure. This targeted innovation combined with a strong emphasis on reliability and service has made virtually all of Fanuc's products blockbusters. While serving completely different, cyclical markets, Fanuc reminds us of Apple in its product approach.

In its core Factory Automation division, Fanuc has capitalized on structural growth in automation by creating a huge moat in Computerized Numerical Control ("CNC") systems and servo motors. It has become the global standard for machine tool control software and motors with a worldwide market share of 60%. The Company has built a global service/aftermarket support organization that is unrivaled by competitors in a business where switching costs are high. The division's revenue correlates closely to Japanese machine tool orders, which are on the rise for multiple reasons including strong demand from the US and a depreciating yen. Additionally, Chinese factory automation is a substantial growth opportunity as rising wages, low productivity, and quality issues force companies in the region to automate. To get a sense of the opportunity: China's CNC penetration rate of 30% today equals Japan's levels 40 years ago. Fanuc is expanding CNC capacity by 40% in the next twelve months to meet these higher demand levels.

Fanuc's Robots division has achieved a cumulative sales growth of 60% in the past two years, capitalizing on a robust opportunity set across all major economies. In China, automotive industry robot density is still at less than 15% of the levels seen in Japan, while general industry robot density is at less than 5% of Japan's. In Japan, capital equipment replacement demand, some re-shoring of manufacturing and labor shortages are creating multiple drivers for robot demand. The resurgence in US manufacturing is also providing strong demand, as automotive and general industry customers are increasing orders for lifting, picking, welding, painting, and dispensing robots. Virtually every large manufacturing footprint expansion in North America – from Airbus to Ford to Tesla – is taking place with Fanuc's robots. Fanuc's internal development of low cost full artificial vision systems and collaborative robots makes it best positioned to drive adoption in industries that have traditionally been unable to automate. We think that these innovations will double the size of the Robots division in only a few years.

Finally, Fanuc's Robodrill product, a small CNC machining center, is a great example of how the Company consistently becomes the manufacturing standard in new industries. A relatively obscure product a few years ago, used only by Apple in its unibody metal casings process, the Robodrill has grown sales six-fold over the past five years. Apple is now using the Robodrill for all of its products and has driven many of its competitors (Samsung, Xiaomi, etc.) to do the same. Due to fragmentation and Fanuc's cost competitiveness, there is no machine tool company in the world that can step in and create incremental supply sufficient to diminish the profit pool of rising demand, a phenomenon we have seen repeatedly in the semiconductor industry. Fanuc stands to benefit greatly as metal casings become the standard for most smartphone manufacturers and Apple's CNC replacement cycle takes hold.

Fanuc's productivity is among the highest in the world, on track to achieve $2.4 billion of operating profit and 40% margins in FY14 with just 5,500 employees. It is generating 25% more income per employee than Goldman Sachs. This can be explained not only by its dominant market position and significant pricing power but also by the fact that Fanuc practices what it preaches – it uses robots to manufacture everything it sells in assembly plants at the foot of Mount Fuji that run 24/7. Furthermore, this highly automated manufacturing platform has unparalleled vertical integration, as CNCs and servo motors are used internally for robots and Robodrills, allowing Fanuc to amortize its fixed cost base and generate a return on capital in excess of 40%.

There is a reason that Fanuc remains cheap at 13x FY15 earnings: the company's illogical capital structure which does nothing for shareholder value. Fanuc has $8.5 billion of cash, 44 million treasury shares (repurchased from Fujitsu) and no debt, which is hard to understand given the company's business quality, growth opportunities and low capital intensity. Furthermore, because Fanuc as a rule does not communicate with investors and sellside analysts, its future earning potential is obscured. We believe the stock could rerate significantly if a buyback program was initiated, which the company has done in the past and would be consistent with a trend we have recently observed at a number of far less advantaged Japanese companies.

Greece Update

In 2014, Greece's economy started to improve modestly after a long malaise. This progress proved to be too little too late for Greece's former Prime Minister, Antonio Samaras, whose New Democracy party was defeated in January elections which were triggered by the parliament's failure to elect a President in December 2014. Samaras was committed to keeping Greece in the EU and had implemented unpopular but necessary fiscal and structural changes to pull the country back from the 2012 brink. Greek voters, who had suffered from austerity just long enough to miss out on its emerging benefits, rejected his approach and elected Syriza, a popular but inexperienced leftist party. Syriza's first move was to form a coalition with a radical right wing party with whom they shared one key interest: aggressively confronting the Troika. The markets naturally reacted with grave concern.

Today, the situation is changing daily as Syriza finds its footing and faces divisions within its ranks. As we have seen many times before, campaigning and actually governing are two completely separate things and unfortunately, in this case, there is no time to learn on the job. The government is currently dealing with a plunge in asset values and tight liquidity for both the sovereign and banks. Tax collections – a significant, if unpopular, focus of the former PM – slowed significantly in the past few months, putting fiscal pressure on the government. Over the last few weeks, Greek banks have needed to borrow emergency ECB funding at high costs in order to meet deposit outflows. We believe that unless an agreement with creditors is reached this month, Greece will begin experiencing extreme liquidity pressures in early March. These liquidity pressures will only escalate leading into April as government treasury bill obligations and interest payments/maturities to private creditors and the IMF begin to pile up. Greece theoretically has enough liquidity to make it through February and possibly March (absent a bank run) but as we have witnessed time and again, the path to insolvency starts slowly but ends very quickly.

Thus far, Syriza has appeared unwilling to adjust its negotiating strategy to these liquidity constraints, instead choosing to remain firm on campaign pledges not to extend the current Troika program. This will soon create a "between a rock and a hard place" moment since Greek voters did not mandate Syriza to take Greece out of the Euro or default on its debts. The country's only liquidity source is its EU partners, who will insist on continued monitoring and reforms as a funding condition. Syriza is far from omnipotent – it does not have a majority in parliament and its coalition is viewed as relatively weak given that its partner finished sixth in the elections, with less than 5% of votes, meaning only about 40% of voters voted for this government. A potential outcome of failed negotiations is a collapse of the existing coalition and possibly new elections, which would create significant market volatility but most likely produce a national unity government with a clear mandate to prevent catastrophe.

Despite this chaos, on the other side of the table, no one wants a Greek exit ("Grexit") from the European Union. We are confident that Germany believes funding Greece and reducing its debt through a politically palatable restructuring is a good investment of German taxpayer funds. In 2014, Germany is poised to break the world record for largest current account surplus (again) at a whopping ~$285 billion, nearly double that of China and triple that of Saudi Arabia. Germany also boasts Europe's lowest unemployment rate at 4.9%, which is half the Eurozone average and one fifth that of Greece. Both Germany's current account surplus and low unemployment are enabled only by an artificially low currency which would be threatened with extinction should any Eurozone member opt – or be forced – to leave. As one German politician recently said, "Have you seen what happened to Switzerland?"

These are powerful incentives to drive a constructive German negotiating position, but the German government will not be blackmailed or embarrassed. Greece and Europe should almost certainly find common ground if Syriza can provide real alternatives to Greece's existing austerity measures while respecting Germany's need for a politically acceptable outcome. What a Syriza-led government ultimately means to Greece's economic prospects remains unclear but one thing is certain: if they do not play their cards well in coming weeks, it's likely we will never know.

Sincerely,

Third Point LLC

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