



MASSIFCAPITAL

January 5th, 2018

Dear Friends and Investors,

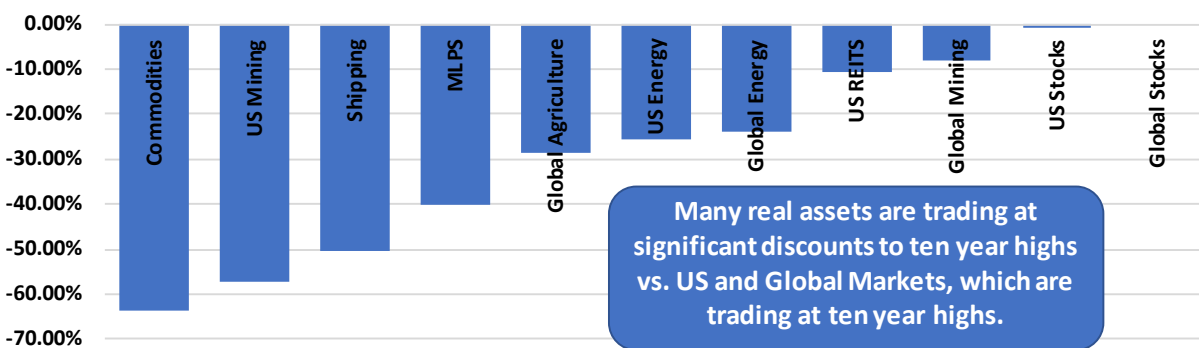
For the quarter ending December 31, 2017, the core portfolio was up 8.8% net of all fees and expenses compared to 5.6% for the MSCI All Cap World Index. In 2017 the core portfolio was up 6.0% net of all fees and expenses compared to 22.0% for the MSCI All Cap World Index. Since inception in June 2016 through the end of 2017, the core portfolio has returned 24.3% net of all fees and expenses compared to 32.2% for the MSCI All Cap World Index. Returns in separately managed accounts may differ from the core portfolio based on initial investment date.

Year End 2017 General Commentary

In general, our approach to securities valuation prioritizes balance sheet strength and businesses as they currently are, rather than a valuation based on forecasts of potential growth. This focus means our investments prioritize companies with real and productive assets on their balance sheets. Historically this has been a profitable portfolio tilt as real asset equities have generated an average return of 7.7% annually since 1991 vs. 6.7% for global stocks overall.¹ Since the financial crisis, the roles have been reversed though, making our investment focus a more difficult path. Combined with a commodity bear market and low inflation, returns on real asset equities from 2010 to 2015 have hovered around 1.0% vs. 7.1% for stocks in general.

Nevertheless, we must remain consistent in our approach to investing. Departing from our balance sheet focused value strategy, in favor of a growth or momentum strategy, for example, would be a grave error in judgment. Given that many real asset companies are trading at significant discounts relative to their ten-year highs (see Figure 1) a shift in our approach would seem particularly poor judgment. From our perspective in the equity trenches, the ground is shifting, and multiple catalysts for unlocking the value of real asset equities are on the horizon.

Figure 1: Current Price of Real Asset Equities vs. 10 Year High



Several real-asset positive macroeconomic trends are worth noting, including the transition from fiscal austerity to fiscal expansion, synchronized global growth and the global rise of protectionism.

¹ May 21, 1991 to December 21, 2016. Real assets are measured via an equal weight blend of real estate securities, commodities, global natural resources equities, industrial and global listed infrastructure.

- The recent U.S. Tax bill, whatever its shortcomings, is an example of expansionary fiscal policy we are starting to observe around the globe. Although we are uncomfortable with the idea that austerity was ever a reality in the post-financial crisis era given the growth in government debt, politicians believed it was the case, and now appear ready to loosen government purse strings. The U.S. administrations intent to push through a large infrastructure package in 2018 appears likely. Outside the U.S. we see similar trends. The rise of European populism, despite recent political setbacks for the populists in elections in France and Germany, is likely to drive looser budgets, not tighter.
- Years of tepid global growth appear to have given way in 2017 to a synchronized and accelerated pace of growth throughout most of the globe. In the US, the trend started in mid-2016 and accelerated following the presidential election. In Europe, improved business confidence and increased consumer consumption are supportive of the current positive economic trends. Emerging markets continue to outperform economically. Strengthening developed-market currencies may create issues for Emerging Markets countries, but that has not yet been the case.
- The backlash against globalization and the rise of protectionist rhetoric appears likely to push governments to at least try and increase tariffs and tighten up immigration control. The impact of government action on the economy is always uncertain, but both actions have historically led to higher labor costs and higher prices on imported goods. Protectionism often results in a less efficient economy, supply constraints and eventually inflation. Over the last thirty years, globalization has been a deflationary force, the shift towards increasing protectionism and slower global trade would seem likely to throw this process into reverse.

The macroeconomic backdrop described above, combined with stretched valuations in many technology, financial, healthcare, and services businesses, would appear a constructive environment for our current portfolio and focus. One of the unifying characteristics of many of the real asset businesses we are invested in and continue to look at, is that they tend to outperform in inflationary environments. Inflation has not been a significant consideration for most investors in recent memory: globalization, declining interest rates and slowing economic growth are typically deflationary.

The current uptick in economic growth, should it be sustained, combined with a tight labor market and fiscal stimulus are all supportive of inflation. While we are not predicting rampant inflation in the near term, we do believe it will make an appearance in 2018 and could prove to be an impactful variable in 2019 and beyond. We are confident that this represents a multiyear tailwind for the types of investments we make.

Despite the relatively positive outlook presented above, we remain bearish on developed equity markets overall. Skepticism in the power of central bankers and their understanding of the economy is at the core of our bearish outlook. Doubt in the omnipotence of the Central Bank crowd is often voiced in the media and elsewhere, but is a little acted upon sentiment, hence the spectacular rise in equity markets over the last year. During the fourth quarter of last year, we read *The Power of Gold: The History of An Obsession*, by Peter L. Bernstein. Central Bankers were not the focus of this informative read, but they did play a significant role. Unfortunately, the many Central Bank characters rarely ever seemed to play a positive role, they mostly stumbled with policy at every turn for close to two hundred years. Even under the simpler Gold Standard, Central Banker influence regularly outstripped capabilities.

The history of Central Bank action would seem to suggest that the ability to influence interest rates for an economy regularly and productively is not within the capabilities of any group of individuals. To think otherwise is a demonstration of not just hubris but a poor understanding of economic complexity. Nevertheless, the idea that Central Bankers have it all under control appears excepted wisdom, and underpins much of the last few years of equity market growth. Unfortunately, it is a wisdom born of short memories. I suspect that many years from now the post 2008-2009 central bank era will be remembered as the single greatest example of intellectual hubris gone wrong in financial markets since the Noble Prize-winning economist of Long-Term Capital Management (LTCM) needed a bailout in 1998.²

Ironically, both the boys of LTCM and the today's Central Bankers mostly run in the same economic circles. Benjamin Disraeli's 1895 observation about the British economy would seem worth remembering at this point: "Our gold standard, is not the cause, but the consequence of our commercial prosperity." This is as true today as it was in 1895. Central Bankers are the result of economic success, not the creators of prosperity.

As one would expect from a value focused fund we seek to buy deeply discounted assets at every opportunity regardless of any vague or imprecise ideas we may have about the economy going forward. That does not mean we do not strive to develop a deep understanding of the wide range of macroeconomic issues that form the back drop to our investments. Investments are not made because of a positive or negative macroeconomic forecast but understanding macroeconomic risks that might imperil an investment is essential.

The discussion of macroeconomic events above is a mixture of positive and negative potential. On the one hand, there is synchronized global growth which has in part contributed to heavily inflated asset prices. We do not expect this to change in the near term. On the other hand, there is expansionary fiscal policy and record high debt levels. We believe this will become problematic sooner rather than later. Perhaps even more troubling is that traditional methods to combat a downturn through either fiscal or monetary policy may be unavailable or prove ineffective. The confluence of conflicting signals combined with a rather pessimistic view of our policymakers' ability to steer us away from the cliffs, makes for a difficult investing environment. We foresee the next 18 to 24 months being much more complex than the last, which was itself a difficult period for most value investors.

In the short term, the next 6 to 12 months, we are looking to put money to work in a combination of Emerging Markets and global special/event driven situations. In the Emerging Market space, we will continue look for opportunities to buy deeply mispriced assets that will yield multiyear returns in excess of 12%. These types of situations are increasingly difficult to find given current market valuations. As such we will also look to generate a greater percentage of the years returns from special/event driven situations. These investments will generate smaller returns than our long-term buy and hold investments but with comparably less uncertainty given the hard catalysts.³ We are also looking to expand our short book and continue to tailor our rolling S&P 500 put position to best hedge the portfolio against any significant market correction; an event that seems increasingly likely in the next 12 to 18 months.

² For those unfamiliar with the Long-Term Capital Management story I suggest "When Genius Failed" by Roger Lowenstein. For those interested only in the highlights, they levered the fund up 25 to 1.

³ Note that we are not suggesting special/event driven situation investments are less risky only that we consider them to have relatively less future event related uncertainty.

In the long-term, beyond the 12-18 month period, we believe the portfolio is primed for success. Positions are trading far closer to record lows, often below 2008-2009 levels, then they are the record highs of the rest of the market. Every position has a conservative balance sheet and many have the potential to benefit from a pickup in inflation should it come to pass, as we think it will.

Year End 2017 Portfolio Commentary

At the current time, the core portfolio is 80.0% invested with 20.0% of the portfolio held in a mixture of cash and US Government T-Bills. Most separately managed accounts are 61.5% invested, with the largest difference from the core portfolio being a single position in CNX Coal Resources.

The core portfolio holds equities and options traded on Exchanges in the US, France, Singapore, and Canada. The portfolio is 57% invested in United States, 14% in Africa, 8% in Europe, 8% in Asia and 13% in businesses with global operations. The global nature of the portfolio means we also hold positions in a multitude of currencies including US Dollars, Canadian Dollars, Euros and Singapore Dollars. The FX exposure has been a positive for the portfolio, but only in a very small way. We are cognizant of our unhedged FX exposure and always thinking about its positive and negative attributes. At the current time, we see no reason to hedge away the FX exposure. From an industry perspective, the core portfolio is 26% invested in energy, 14% in mining, 8% in financials, 21% in diversified conglomerates and 10% in consumer cyclical's, with an average position size of 8%.

Individual Positions

At the current time, the portfolio is made up of ten equity positions, three options positions, cash and U.S. T-Bills. As we reviewed each position in the 3rd Quarter Letter at length, we will forgo any general description of the positions and only provide updates on position status since the end of the 3rd Quarter.

Barnes and Nobles Education (BNED): BNED recently reported excellent results at the end of their 2018 2nd Fiscal Quarter. Not only was quarterly revenue per share a record but it was 14% above the previous high set during the fourth quarter of fiscal-year 2016. Equally important, BNED broke the three-quarter trend of negative free cash flow, earning roughly \$5.13 a share during Q2-2018. Management's presentation during the quarterly call was more open and informative than past calls with a far clearer discussion of the long-term strategy of becoming a multi-channel distributor of education materials coming into its clearest focus since the company's IPO in 2015. We believe that the progress made rationalizing the business model and managements demonstration of that progress to investors during the call was an important milestone that suggests our investment thesis is on track. Although a pullback in the share price is likely in the short term given the strength of the recent positive move, we believe that operational results should continue to improve over the next 12 months and with that improvement a continued price appreciation of the stock.

Bollre (BOL): Bollre CEO Vincent Bollre continues to make waves with aggressive actions in the European Media space through Vivendi, which is now a consolidated entity on the Bollre balance sheet. Unfortunately, Vivendi is a constant distraction from the excellent African ports business. Our preference would be to own just the African port business, a preference which may led us to divest the entire position out of concern for the long-term potential of Vivendi. Should we hear more about a rumored spin-off of Universal Music Group our outlook for Vivendi may change but only in the near term. In the long term, we have become skeptical that Mr. Bollre has what it takes to right the European media conglomerate. The logistics and port business remains desirable.

CNX Coal Resources (CCR): Production and domestic sales continue to be steady and predictable, while international markets continue to pad the bottom line with strong spot market pricing for the high-quality coal that CNX mines. The dividend of roughly 14%, or \$2 per share per annum, remains easily covered out of FCF, which has averaged \$2.30 a share per annum. Although Coal continues to be a tough business, with limited to no growth prospects, CNX management has effectively run the business for cashflow generation, much of which is returned to shareholders. As such, CNX remains an excellent income investment. To date, management has returned roughly 38% of our initial investment via quarterly dividends on top of a 56% appreciation in the value of the stock.

Diamond Offshore (DO): 2017 was an extremely volatile year for DO, our position has swung from being down more than 20% to up more than 30%. The firm's very aggressive move higher during the 3rd and 4th quarter has resulted in it becoming the portfolio's largest position at roughly 12.6%. By operations and cash flow, the business is worth significantly more than it is currently trading. Based on the number of tenders and prices received for offshore work during 2017, it looks to us like the 2017-2018 period represents a potential end of the downcycle in offshore oil and natural gas. A return to growth in 2018 seems unlikely but will depend on oil price action. Should oil remain above \$60 we could see the rapid appreciation of DO during the 3rd and 4th quarters of 2017 continue during much of 2018.

Global Logistics Properties (MCO): The shareholder vote to approve a management-led buy-out of Global Logistics Properties occurred at the end of November 2017 and was overwhelming in favor of the privatization. Shares are expected to stop trading on the Singapore Exchange just after the new year (January 4th), and cash payments of S\$3.38 per share will be made to all shareholders by January 19th. Barring any unforeseen last-minute events, our return on this investment will be roughly 4.0% in five months, an annualized return of 9.68%. We will be very actively hunting for more opportunities like this in 2018.

Haw Par Corporation (H02): Haw Par was a new addition to the portfolio in the 3rd quarter of 2017. You should all receive a research note on it with this letter. We will be presenting the idea at the MOI Global 2018 Best Ideas Conference next week and will arrange access to that presentation for all the funds investors.

Lucara Diamond (LUC): Lucara continues to be one of the more fascinating companies in the portfolio. Not only is the value proposition clear but the company has recently released a preliminary economic assessment of the mine that more than doubles its life. The balance sheet is pristine and cash heavy, management is cognizant of the value of their current asset and have stated a preference for returning cash to shareholders should they not find an asset that is as value accretive as the existing mine. A tall order given the uniqueness of the Karowe mine. We are conscious of the fact that cash-rich balance sheets have often been squandered by impetuous management but are confident this will not be the case with Lucara.

Nevsun Resources (NSU): Nevsun has struggled significantly this year, and so just before Thanksgiving, we decided to visit management at the future site of the Timok Copper-Gold mine in Serbia. Although operational setbacks at Bishia, the company's Eritrean based Copper-Zinc mine, have resulted in a slight impairment of value, management's decision to prioritize Timok rather than Eritrea appears prudent given the economics of the two projects. Nevsun is undervalued, of that we are confident, but we did error in our initial overvaluation of Bisha and as a result, failed to insist upon a large enough discount to

intrinsic value when we first made our investment in the company. More patience was called for before establishing our position, improving our buying skill is a focus of the coming years improvement efforts.

Och-Ziff (OZM): We invested in Och-Ziff initially with the belief that the future had fewer uncertainties for the company than the rest of the market believed. Thus far our thesis has been correct, but strong portfolio returns and positive action on the part of management to correct areas of managerial weakness have gone unrecognized by the market. Unfortunately, the only statistic that the market appears to care about is AUM. Given the volatile nature of the return profile for Och Ziff, the fact that the assets walk out the door every evening and the laser focus the market has on a singular statistic we are increasingly skeptical that this is a good company for us to be invested in. It seems increasingly likely that the return will be limited and the time line long, as such we no longer believe OZM is the highest and best use of capital, we have begun divesting ourselves of the position this week.

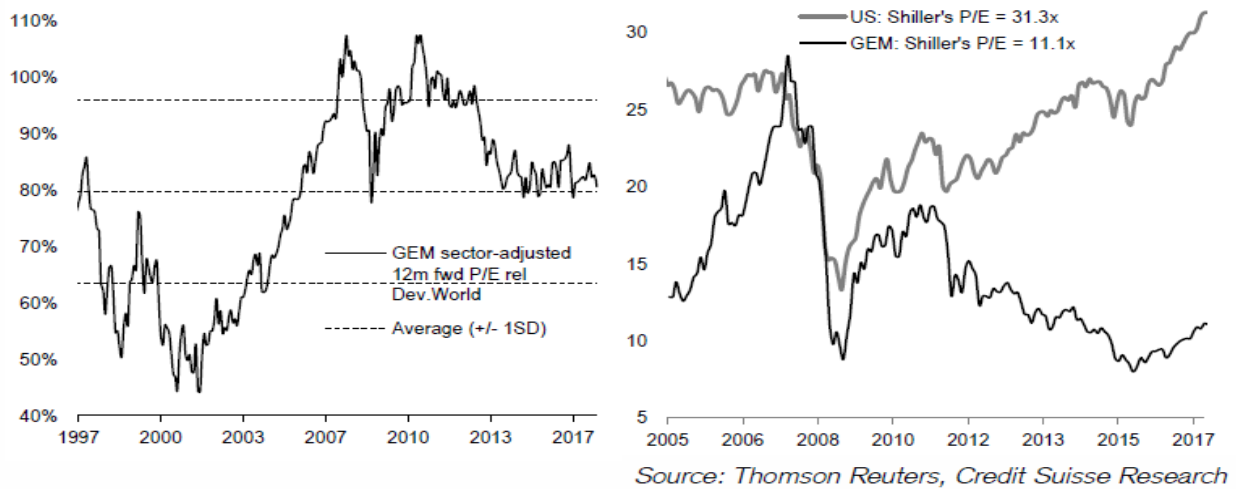
Steel Partners (SPLP): Steel Partners produced a solid return for the portfolio early, returning 15% to 20% within the first few months of investing, but has since done very little. Management has resolved several of the outstanding issues that the company faced when we first invested and the company appears positioned for growth in the near to medium term. Reevaluating our thesis and price targets, in light of the positive changes at the company over the past 18 months, is a top priority, especially given the potentially positive impact of the corporate tax overhaul on the company's bottom line. The potential of this underappreciated conglomerate remains significant.

Looking Ahead

As some of you may already know, Massif Capital has recently doubled in size with the addition of Chip Russell to the team as a partner. Chip has been working behind the scenes for a few weeks now but started full time on January 1st. He brings with him a wealth of knowledge about energy and electricity markets and significant real-world expertise in the battery industry, something we hope to put to good use in the future as that industry matures and grows in importance. Chip will initially focus on fundraising and client services but as time goes on we look to achieve a more balanced division of research, fundraising and client service responsibilities.

Looking ahead to 2018, we will continue to investigate unloved and overlooked industries, at the current time we are most interested in shipping, parts of the mining world (gold, uranium) and emerging markets, with special attention paid to Africa, Singapore, and Southeast Asia. Our Emerging Markets focus warrants a longer treatment, but demographics and the continued maturation of Emerging Market economies are trends at the core of our positive outlook. Complementing the macroeconomic backdrop, are favorable equity valuations relative to developed markets. At the current time, Emerging Markets appear to be the best hunting ground for undervalued assets, see Figure 2.

Figure 2: Recent Performance of Global Emerging Markets (GEM)



We are also conscious of the fact that our portfolio is all long positions despite our relatively unconstructive outlook for equity markets as a whole in the near term. We continue to add to the long book when and where we find good opportunities but are very actively looking for opportunities on the short side.

As always, we appreciate the trust and confidence you have shown in Massif Capital by investing with us. We know that entrusting hard-earned capital to a young emerging fund is difficult and hope that you will never hesitate to reach out if you have any questions or concerns about what we are investing in.

Best Regards,

Will Thomson

Chip Russell