August 28, 2020

Dear Partners,

SRK Fund I, LP appreciated +44.80% during Q2 of 2020. In contrast, the S&P 500 and the Russell 2000 gained +20.54% and 25.50%, respectively. Year to date the Fund has appreciated +47.37%.

SRK Fund I, LP Returns (%) as of June 30, 2020

	Q2 2020	YTD	2019	2018*	Since Inception*
SRK Fund I, LP	44.80%	47.37%	77.99%	2.90%	168.02%
S&P 500 TR	20.54%	-3.08%	31.48%	-4.03%	22.31%
Russell 2000	25.50%	-12.96%	25.52%	-11.72%	-3.75%

**Inception date of 05/01/18*

Most of our portfolio holdings increased markedly during the quarter as pessimism turned to optimism in late March. As always, I remind partners to not project our quarterly returns into the future, and to judge our success over years not months. Although our returns seem surprising compared to the indexes, it can be explained for two reasons. First, our portfolio is considerably concentrated in a small number of holdings and does not represent or mimic an index. Second, most of our holdings have increased their intrinsic values during the first half of this year and their stock prices have followed as warranted.

The Market

People love stocks again, many for their very first time! From a personal perspective, before now, I have not experienced this much interest in individual stocks by those who know extraordinarily little. Many are purely gambling on stocks and typically their main reason for owning a certain stock is based off the story or the idea of the company with little attention paid to the actual business fundamentals. This certainly has caused pockets of speculation to develop in the market. At some point multiples paid do matter; companies do not grow exponentially at the same rates forever. We have reached the point where future growth prospects for companies are being underwritten into valuations without much proven success of those ventures. Businesses do hit speed bumps, and when you pay 40x earnings for a business those hiccups are scrutinized to a higher degree than at a lower multiple of earnings. Sentiment can change on a dime. The higher the multiple, the more significant the moves in interest rates matter. Investment in a stock with an earnings multiple of 40 will be much more sensitive to interest rates than investment in a stock with an earnings multiple of 10. With that said, the Fed has indicated they intend to keep interest rates at the zero bound for years into the future and let inflation run hot. What does this mean? I am not quite sure, and my batting average for projecting macro conditions has been lackluster, so I will continue to leave that for someone else to interpret. Our strategy leans little on predicting the direction of macro and overall market movements. There are still opportunities in areas that the market is underpricing, especially in corners of the market that we like to search.

Portfolio Updates

The quarter was quite active for the Fund. We had bought and then sold several stocks during the quarter. This is highly unusual for us, but when a stock has several years' worth of a returns in a matter of months, I tend to ring the cash register.

Tile Shop Holdings, Inc. (TTSH)

The Tile Shop is a classic example of forced selling (twice). Here is a brief history on how the opportunity presented itself: On October 22, 2019, the company notified shareholders that a board member was resigning, they were suspending the dividend, suspending the buyback, and voluntarily delisting their shares from the Nasdaq. The result of this announcement was a near 70% decline in the price of the stock. This scenario initially piqued my interest. The company used poor Q3 results to defend the actions that they were taking to reduce costs and improve operations. Over the course of the next month the Chairman of the Board, Peter Kamin, and a director, Peter Jacullo, used the precipitous decline in the price of the stock to increase their combined ownership of the company to approximately 30%. Two shareholders took notice and filed a lawsuit against the company for breach of fiduciary duty in connection with the decision to delist and deregister its common stock; this led to the directors of the board to enter into a standstill agreement that they will not personally purchase any shares of the company's common stock for a period of two years. During depositions Kamin and Jacullo admitted that they knew delisting and deregistering the stock would cause institutions to unload their shares, which would allow them to increase their ownership in the company at a significantly cheaper price, and the end game of the go dark scheme is to turn around and later sell the company. Then the coronavirus hit…and this allowed us to take advantage of a terrific sale. Solely on a balance sheet perspective I believed even with a severe decrease in revenues for 2020 that the company had enough liquidity and levers to pull that it would be able to survive the year and did not deserve to be priced as if it were heading for bankruptcy.

During the second quarter TTSH was able to take the necessary steps to cut operating expenses, preserve cash, and generate cash flow. In the first half of the year, the company was surprisingly able to reduce their debt by ~$40 million, leaving net debt at $14.06 million as of June 30th. Also, the company settled their lawsuit during the quarter for $14.5 million, which will be paid by an insurance policy.

Looking forward, I expect revenues to recover to more normalized levels over the next several quarters as they benefit from the rise in existing home sales and the boom in remodeling that is taking place. I believe the business can be turned around and operations right sized. In the past several years SG&A as a percentage of revenues has increased to about 70%, the company needs to be slimmed down and I believe looking at 2016 and 2017 numbers give a good idea of how profitable the operations can be, when they did $32 and $25 million of operating income, respectively.

Nocopi Technologies Inc. (NNUP)

Nocopi reported a 22% increase in revenues year over year. Product sales increased 61% year over year, which will lead to higher future royalties. The company has been aggressively increasing their inventory this year to keep up with demand as they head into their busiest two quarters of the year. Shares have strongly rallied this year on continued revenue and cash flow growth. Even with the increase in share price Nocopi is still a bargain at less than 12 times earnings. At the moment, there is not much more I can say about Nocopi that I haven't already explained in previous letters to you. I will continue to keep you updated on the company's progress.

IBEX Technologies Inc. (IBT.V)

Ibex's stock increased 123% during the second quarter due to record quarterly numbers. Year over year sales increased 20% and the company has not been negatively impacted by Covid-19. As previously mentioned, during the past year they have shut down their Iowa facility (including selling the real estate) and moved all production to their Montreal facility, projected to save about $700,000 a year in expenses. This reduction in expenses is continuing to show through on the income statement as operating expenses decreased nearly 11.5% from a year ago. Ibex recorded Ebitda of $769,335 during the quarter compared to a loss last year. Cash on the balance sheet now stands at $2,843,130 representing 63% of the market cap. Ibex is one of the cheapest stocks I know of trading for less than 2 times cash flow.

Pershing Square Holdings Ltd. (PSH.AS): Pershing Square is the publicly listed fund managed by Bill Ackman. The portfolio includes the likes of Berkshire Hathaway, Chipotle, Restaurant Brands (Burger King, Popeyes, and Tim Hortons), Agilent, Lowes, Hilton, Howard Hughes Corp, Starbucks, and several others. Pershing has performed exceptionally well so far this year up more than 40%. Even with that performance the fund still trades at around a 30% discount to NAV. I know Ackman is controversial at times and has made some fairly large mistakes in the past, but his performance is still remarkable. I believe Pershing's renewed strategy on investing in high quality companies removes most of the "blowup" risk that might be hanging over his head leading to part of the reason for the discount to NAV. As the market eventually comes around to the viability of Pershing's strategy and the fund continues to buyback its own shares the discount will eventually narrow. I feel the fair discount to NAV should be somewhere around 10%; some may even argue it could trade at a premium to NAV.

Feel free to reach out to me regarding further explanations about any of our holdings. I look forward reporting back sometime after the third quarter.

If you or someone you know is an Accredited Investor and would like to learn more about the Fund please reach out to us at info@srk-capital.com and we can set a time for a more detailed discussion to determine if we are a good fit.

Sincerely,

Sean Kirkwood

SRK Capital, LLC