Long Cast
ADVISERS LLC

Dear Friends:

Cumulative returns on accounts managed by Long Cast Advisers decreased 7.4% in 2Q18, net of applicable fees. This was worse than the various indices against which we benchmark ourselves. Returns for separate accounts managed by LCA ranged from -6% to -9% for the quarter.

Year to date returns through June 30, 2018 is (8.6%) net of fees. Since inception, we have returned a cumulative 61% net of fees, ahead of our benchmarks.

PERFORMANCE

	LCALLC Gross*	LCALLC Net	R2000	S&P	Dow
	Annual Percentage Change				
2015 (2-mos)	12%	12%	-5%	-2%	-2%
2016	17%	16%	21%	12%	17%
1Q17	10%	10%	2%	6%	5%
2Q17	2%	2%	2%	3%	4%
3Q17	9%	8%	6%	4%	6%
4Q17	13%	12%	3%	7%	11%
2017	38%	36%	15%	22%	28%
1Q18	-1%	-1%	0%	-1%	-2%
2Q18	-7%	-7%	8%	3%	2%
YTD	-9%	-9%	8%	3%	0%
Cumulative chg	64%	61%	42%	37%	46%

This has obviously been a challenging year to date. Many of our newer purchases are under water and most of our top holding across all accounts are down for the year.

A little more than two years into running my business, following the first substantial portfolio turnover (three companies were acquired summer '17) and concurrent with growth in my client base and AUM, I am getting the kind of setback Mike Tyson might have been referring to when he said: “Everyone has a plan until they get punched in the mouth.”

Short term price performance is always a major factor impacting results. We own companies for the long term and I believe there is the opportunity for value recognition in our holdings over time, given their valuations, end markets, services, products, management and financials.

However, there are also lessons buried in 1H results that can help improve investment discipline, portfolio construction and marketing, so that clients can be best served and my firm and our portfolios can endure and grow into the future.

I’ve always taken an incremental approach and will continue to do so here but I’d be a fool to let valuable lessons go by. So I want to share a few reflections on quarterly and YTD results.

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Things I Want

More patience. I view stock ownership as something akin to a marriage; make sure you have the right partner, buy the right small company, and stay with it for a long time. Divorce (via loss of capital or even the tax consequence of selling) can be expensive. That's why I spend a lot of time on due diligence.

What I've observed is that there's a cadence to the business - when money comes in - and a cadence to investing - when I find ideas that are worthwhile to own at the right valuation - and I can't force them to align. One of the reasons newer clients have larger cash balances is that I am patiently seeking new investment ideas.

A checklist, to avoid error and pursue consistency and repeatability. In the past I wrote, "... I am cautious of detailed checklists, b/c it risks creating a false impression that on completing it, we'll have certainty."

I've reflected on this, took a trip to The Strand, bought Atul Gawande's book, and now recognize something I'm sure many others already know; checklists aren't intended to assure optimal outcomes but to avoid errors.

I want to grow capital without taking on unnecessary risks. I also want consistency and, as much as possible, given my qualitative approach, repeatability. I think a checklist can help with these by improving discipline in the overall investment process to ensure I don't "skip steps" and by adding deeper nuances to the winnowing process.

I'll expand more on checklists in the future but as I think about it now, it will include procedural steps, enforced pause periods and efforts to better identify imbalances and misalignments.

More small-and-focused companies. I continue to want to own companies that are or have an opportunity to generate copious amounts of cash and reinvest it at high rates of return, while avoiding hydrocarbons and weapons. They come in many shapes and sizes, as platforms, as distribution models, as manufacturers or services, as fixed capital owners with operating leverage, as royalties, as bulk breaks, as local operations or even at global scale, just to name a few.

But I've come to realize that the best ones are focused. When management's center of attention is directed towards solving a specific set of tangible problems for customers (ie not for themselves) at prices customers want to pay, and the stocks of those companies trade at valuations that offer material upside to a reasonable investor, then everyone wins.

More marketing experiences. Having my first institutional client has opened doors to more institutional engagements and at my first institutional "sales meeting", I pretty much fell on my face. Thinking it would be like an analyst meeting (which I've done hundreds of times in my career), I was 100% prepared … for the wrong meeting.

Potential clients are not looking for me to regurgitate what I like about the stocks I own. *They are looking for a repeatable process and discipline*. These things are hard to convey with a qualitative investment process like mine, but over time, it's something I think I can get right.

I owe an enormous amount of gratitude to two people following the meeting.

1. The client, who when asked, was kind enough to provide material feedback and constructive criticism.
2. Brian Bares, not just for writing his book but also for sharing in this video 1 minute 30 seconds of a story about his first institutional presentation, which offers fine company to my misery.

The key thing I learned, from this experience and from friends in a variety of fundraising fields, is that the goal of a meeting is simply to have another meeting in the future, with the idea of developing a long term relationship over time. Full stop. I look forward to more of these meetings.

Things I Don't Want

Companies run by value destroyers. With our current investments, what eats at me most are the things I overlooked when the stocks were initially purchased. I view myself as a patient investor who does deep due diligence on the front-end in order to feel comfortable owning assets for the long term, so it's painful to find simple things I missed.

Which is why, even though CTEK was the quarter's worst performer (it tends to generate the bulk of its profits in 2H), Invuity hurts the most. I wish had weighted more heavily the value destructive tendencies of its prior CEO, Phil Sawyer, in his prior role at Fusion Medical. Thankfully, he is now gone, (not long after we wrote a letter to the Board).

I believe the new CEO, Scott Flora, deserves a chance. This is not his first time running a small company. Interestingly, in talking with people he worked with at Omniguide, it's clear he had some issues translating his prior successes at larger firms (Covidien, Smith & Nephew) to a smaller firm. It sounds like the biggest issue had to do with resource management (ie recognizing that small companies don't have the same resources as large companies), not an uncommon experience for people in many fields who make that transition.

Based on what I've heard, he is an excellent, customer focused salesperson, and IVTY has long been missing this. They already have a well-regarded portfolio of products. The company does not need substantial R&D to win, it just needs to get its sales right. He has already narrowed the company's direct selling focus to the female health market (OB / GYN / Breast) and is using alternative channels for international sales and additional verticals, indicating a center of attention towards procedures with the highest returns, something prior management never did.

There is a path to profitability and shareholder returns; it will take longer than anticipated but the IRR potential remains compelling.

<u>Concentration, for the sake of concentration</u>. Small / micro cap companies are a volatile asset class. Layering concentration increases this volatility. It's wonderful when the stocks go up but it sucks when they go down.

I do not want to distinguish myself by taking on more risk than necessary to generate above average returns. The beauty with small caps is, with the right balance, you can be in a position to make a lot of money if you're right and not lose a lot if you're wrong.

There will be times when it's appropriate to significantly increase concentration, when there are unusual imbalances in valuation relative to operations and / or the balance sheet. Furthermore, since I "let my winners run", there will be times when our long-term holdings organically represent large portions of our portfolios.

But not every opportunity is a great opportunity and great opportunities do not come around all that often. I don't imagine owning +20-companies but I struggle with the volatility that comes from owning only five or six.

<u>A "model portfolio"</u>. It would be incomplete to discuss concentration and portfolio management without discussing one of the unique factors of running separately managed accounts vs a partnership, so here it is. I've tried the "model portfolio" and I hate it.

I do not want to trade stocks. I do not want to arbitrarily rebalance because the calendar says it's the end of a month or year. I do not want to buy at high multiples and at the same concentration for new client X what I bought earlier and at lower multiples for clients A, B and C. I understand the theory and concept of "re-buying what I own everyday" but there are frictional costs (taxes, commissions, effort, timing) in the practice of that theory that make it unwise with small cap companies.

I am much more content with the likelihood that clients may have different portfolios and different returns due to the timing of when they become clients than I am with the need to buy or sell stocks simply because of the timing of their deposits.

Investment partnerships have their advantages (the automatic rebalancing of new moneys) but SMA's also have advantages (much lower costs). I will manage the portfolio on a total consolidated basis and I will own everything my clients do but the most important thing that I aim to do is serve my clients by providing them an opportunity to generate outsized returns on their capital, by owning a portfolio of great companies acquired at reasonable prices.

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NEW POSITIONS

We have been buying three new positions. All have a long history of growing BVPS with limited share dilution. Two are software companies experiencing substantial growth while the third is a capital equipment maker coming off an unprecedented 2017 and therefore experiencing negative comps that weigh on the stock. We continue to buy all of them and so I am reluctant to discuss in detail.

EXISTING POSITIONS

I always expect our managers to patiently operate towards optimal capital allocation. When I see behavior that falls short, I fight for myself and my clients by writing letters. Unfortunately, I have written plenty of letters this quarter, some published here, others sent privately to managers.

In most cases, the goal of a letter is to try to understand the reasons and justifications for certain decisions and to understand what benchmarks an outside investor should follow to assess the quality of those decisions. Occasionally, it's to offer guidance, such as the letter I sent to QRHC suggesting they re-domicile to DE so other institutional investors might take them more seriously. Sometimes it's to advocate for change, such as with Invuity. Sometimes it's to call attention to issues management may overlook, such as DSO's at SIFY. *In all cases, my goal is to stand up for mine and my clients' capital as an engaged shareholder.*

However, the pen offers limited solace. It's my desire to get better at focusing only on companies that are managed by terrific capital allocators, and to let everything else go by.

CLOSING THOUGHTS

Sometimes I feel like I'm in a rush to grow. I look around and see others growing their firms and want mine to grow too. Were I in any other business, I'd likely feel the same way, but this business is different; I can't just produce more widgets. I have to produce better, more consistent, more predictable and more repeatable intellectual capital. I believe implementing some of the things I've reflected on in this letter will support that effort.

As always, I appreciate your entrusting me with your capital and the responsibility associated with being its steward. If you have any comments or questions, please don't hesitate to call.

Sincerely / Avi
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Brooklyn, NY

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