1 MAIN CAPITAL

October 2018

Dear Partners,

During the third quarter, 1 Main Capital Partners, L.P. (the "Fund") gained 3.6% net of fees and expenses[1], bringing the inception-to-date net return of the partnership to 10.1%[2]. Over the same period, the S&P 500 Index (SPX) returned 7.7%, bringing its February-to-date performance to 4.6%[3]. The Fund's performance was held back by market hedges, which cost the fund >2% during the quarter, as well as its cash position, which averaged ~37% of assets over the period. Given the Fund's concentrated portfolio, I do not compare results with market indices on a quarterly basis. Rather, the Fund strives to hold an ownership interest in a collection of high-quality businesses whose values will grow over the long term, and whose performance are not perfectly represented by the price at which they trade on the last day of each quarter. Additionally, while the costs of hedges and excess cash are easy to question during periods where stocks are in favor, these should be viewed as tools that will enable the Fund to deploy cash when the market price for liquidity is high and the return profile of new investments becomes increasingly attractive.

As mentioned in last quarter's letter, the Fund's goal is to generate strong long-term returns while minimizing the risk of permanent capital loss. As such, it is my hope that its results will be judged not on a quarterly basis, but on the Fund's performance over the coming 3, 5 and 10-year periods.

<u>Third Quarter Contributors</u>[4]

The table below highlights the Fund's top winners and losers for the quarter. In this letter I will touch on a few of the positions below, and as always, I'm happy to discuss specific positions in more detail with investors.

Top winners	
XPEL Technologies	2.6%
Undisclosed short	1.4%
Loral Space & Communications	1.2%
Atento	1.1%
Ashford Inc	0.8%

Top losers	
S&P 500 hedges	-2.1%
Facebook Inc	-1.1%
Tenet Healthcare	-0.5%
RCI Hospitality	-0.4%
Dynavax Technologies	-0.3%

XPEL Technologies (DAP.U), which was discussed in the previous letter, was the fund's largest winner in the quarter. The company continued its impressive growth trajectory in Q2, growing revenue and earnings at 69% and >300% YoY, respectively. Importantly, the strength was broad-based across most of the company's geographies. The company's primary product is still used on only a single-digit percentage of cars and is expected to benefit from continued expansion of its application over time. At quarter end, the company was being valued by the market at approximately 19x and 12x run-rate and estimated 2019

[1] Performance data is presented for the Fund's Class A Interests, and is net of any accrued incentive allocation, management fees and other applicable expenses (as disclosed in the Fund's Confidential Private Offering Memorandum), include the reinvestment of dividends, interest and capital gains, and assume an investment from inception. Returns for month-end and year to date 2018 are estimated, and un-audited. For investor specific returns, please refer to your capital statements. Due to the format of data available for the time periods indicated, net returns are difficult to calculate precisely. Please see the last page for important disclosure information.

[2] 1 Main Capital Partners, L.P. commenced trading in February 2018.

[3] Source: Bloomberg

[4] Attribution is presented gross of management fees, expenses, and incentive allocations.

earnings, respectively, an attractive valuation considering these growth rates. Additionally, given the company's recent increase in market value, XPEL has begun exploring ways to broaden its investor base, including by uplisting to the Nasdaq or NYSE.

Loral Space & Communications (LORL) is a $1 billion holding company whose primary asset is a 63% economic interest and 33% voting interest in Telesat, a Canadian satellite company. Since Telesat, the operating business, is not controlled by LORL, the holding company, it is not consolidated into LORL's financial statements. This causes LORL's stock to screen poorly. Additionally, 40% of LORL's float is held by a single shareholder, a feature which causes many investors to pass due to liquidity constraints. It is because of these dynamics that the Fund was able to initiate a position in LORL at an attractive valuation, especially given some key potential catalysts on the horizon.

Telesat operates a fleet of satellites that it leases to video distributors, telecommunications companies, governments, and other enterprise users. Given its stability, the company can operate with modest leverage of $2.3 billion of net debt and $575 million of trailing twelve-month EBITDA, while still generating ~$250 million of free cash flow per year. At LORL's quarter end share price of $45, the market is implying that Telesat is worth 7x EBITDA and a 15% levered free cash flow yield, which is a significant discount to the $80 per share bid LORL turned down in 2014 from PSP and Ontario Teachers'.

In addition to this appealing valuation on the core satellite business, Telesat's potential monetization of C-band spectrum and its launch of a new LEO satellite represent two opportunities that could provide meaningful incremental upside to current trading levels.

> C-band: Telesat has a low single digit share of C-band spectrum in the US, which the FCC is keen on freeing up for 5G wireless use. Recently, Telesat joined three other satellite operators (Intelsat, SES and Eutelsat) to formalize the creation of the C-Band Alliance, a group established to facilitate the transfer of some C-band spectrum from satellite operators to cellular operators in the US. So far, the FCC appears to be onboard with the idea that members of this alliance should be compensated for clearing this airspace. While the range of potential proceeds that these members may receive for clearing the space is wide, some estimates imply LORL's portion could be multiples of its current share price. In anticipation of a potential C-band auction in the coming year, SES's and Intelsat's stock prices have appreciated 60% and 900% year-to-date, respectively, while LORL's stock has been flat.
>
> LEO constellation: Telesat is working on designing and building a new Low-Earth-Orbit (LEO) constellation. While the company has been reluctant to provide exact details on the project for competitive reasons, they have made it clear that they expect it to be a significant value driver. In October of 2017, the company stated that it was in discussions with potential partners – both strategic and financial – to finance the buildout of its LEO constellation, which could end up consisting of >500 satellites. In January of this year, the company launched its first prototype, which secured its position through the ITU and gave it priority rights in the Ka band. As more details emerge regarding the company's ambitious LEO buildout, I believe that investors will start to recognize the significance of the opportunity relative to the company's current market valuation.

While the above call options alone are enough reason to own the stock, LORL may also be getting closer to resolving its liquidity and holding company overhangs. In 2015, LORL exercised its right under its agreement with Telesat's controlling shareholder to request that Telesat to initiate an IPO. With the IPO being delayed for an extended period of time, LORL added language to the risk section of its 2016 10-K stating that it is being held up by Telesat's controlling shareholder, but that LORL may further pursue this right "in the event a combination transaction or a sale of Telesat is not likely to be achievable in a timely manner or on satisfactory terms." Based on this language and some additional information in the company's disclosures, it is reasonable to assume that Telesat's controlling shareholder is negotiating with LORL to either collapse the two share classes into one, or to sell the company, either of which should provide a favorable outcome for LORL shareholders.

Facebook (FB) is the social media company that owns and operates the eponymous Facebook platform, as well as Instagram, Facebook Messenger and WhatsApp. Remarkably, each of these platforms has over one billion users. In addition to the company's significant reach, it has been also able to use targeting to significantly increase effectiveness for advertisers, which has in turn allowed it to increase its share of wallet with those customers. This effectiveness is what allowed FB to grow its revenue from less than $1 billion in 2009 to more than $40 billion in 2017, despite generating almost no revenue from Instagram, Messenger or WhatsApp over the period.

Following the 2016 elections, the company came under scrutiny for its handling of user data, and began facing an increasing amount of negative publicity, which accelerated earlier this year driving a major sell off. The company began making substantial investments in the business to regain the trust of its users and to address many of the questions raised by congress and the media. It was clearly taking strides to move past these issues, while advertisers continued to find a highly compelling value proposition in the platform. On its Q1 call in late April, management signaled that it was business as usual and that it was seeing no meaningful impact from the negative attention or from new privacy regulations that were being implemented in the EU. I used the opportunity to build a position in FB in the second quarter. I further added to this position over the course of the quarter as it appeared that the issues were moving further into the rearview mirror and that monetization of the Instagram platform was beginning to accelerate.

However, on its second quarter call, the company further guided down, warning about significant revenue deceleration as well as margin compression. While investors were prepared for additional investment in the business, and I believe would have given FB a pass if this were the only surprise, the speed of the revenue deceleration in conjunction with the magnitude of the margin compression caught the market by surprise. Additionally, management did a poor job of explaining the reason behind the revenue slowdown, especially after giving everyone the all clear signal just a few months prior. In short, their tone change didn't pass the market's sniff test.

Since then, the shares have continued to trade off and are now 30% off the high, as the market debates i) whether management's outlook was conservative or realistic, and ii) whether the revenue deceleration is transitory or structural.

> In support of the case where it is transitory, the company has suggested that it is shifting advertisers towards under monetized features such as Instagram stories, which have less pricing power because their advertising ecosystems are less developed. Additionally, the company has focused on making the user experience on its platform a more positive one by increasing people's exposure to content that causes them to interact with their friends rather simply consume information, which is less profitable in the short run but creates a stickier and more durable

platform. If these are the true reasons for the topline deceleration, they are within the company's control as to how quickly they make this transition and their new guidance is likely conservative.

In the case where it is structural, one can argue that as more users begin to utilize data privacy features provided by the company (sharing less data), advertising on the platform becomes less effective and in turn the outcome is not in the company's control.

I tend to believe that the revenue deceleration is transitory in nature, and that the company is still exposed to i) several powerful secular trends, and ii) a portfolio of under monetized assets. At the same time, the stock trades at a reasonable multiple relative to its expected growth.

With this drawdown off the highs, the Fund has now given back its 0.7% Q2 gain from the position and lost a more modest (0.4)% on position for the year. While the company could become a core position over time, I have reduced the Fund's exposure to the name until I get more clarity on the trajectory of its various properties.

Top 5 Current Positions

As of September 30th, the Fund's top 5 positions were Alphabet Inc (GOOG), Ashford Inc (AINC), Echostar Corp (SATS), RCI Hospitality (RICK) and XPEL Technologies (DAP/U). Together, the Fund's top 5 positions accounted for ~36% of assets, compared to ~25% of assets at the end of the second quarter. This is in-line with my goal of getting more concentrated over time, since the largest positions are the ones I find most compelling. I expect this trend will continue over time as market volatility increases and new opportunities surface. Given the Fund's strategy of looking for long-term compounders and having low portfolio turnover, it should be unsurprising that 4 of the top 5 holdings were discussed in last quarter's letter. Feel free reach out to request the Q2 letter if you do not have a copy.

Ashford Inc (AINC) is a new position initiated by the Fund during the third quarter. This $200 million market cap company provides asset management advisory services to two public REITs, Ashford Hospitality Trust (AHT) and Braemar Hotels & Resorts (BHR). AINC was spun out of AHT in 2014 with the goal of creating value by separating the REIT's property ownership and property management functions.

AINC's advisory segment, which makes up a majority of the company's earnings, is a predictable and stable business:

- AINC's REIT clients pay it a fee of ~0.7% of gross asset value, which currently stands at >$7 billion
- Since 2003, the REITs have grown their assets at a 26% CAGR
- The maximum annual decline in the fee paid to AINC cannot exceed 10%
- The initial terms of the advisory agreements run through 2025, provide for automatic five-year extensions and, if canceled, provide for significant termination payments to AINC

The advisory segment should continue to grow alongside REIT AUM. AHT and BHR's combined $500 million cash balance, in addition to the AINC's contribution under EFRP (described below), should allow the REITs to acquire >$2 billion of assets. In fact, last year AHT tried but failed to purchase another REIT called Felcor which would have grown AINC's AUM by nearly 50%.

While AUM growth represents the company's primary method of growing revenue, it has numerous other proven and potential growth vectors, including:

- AINC drives growth by acquiring businesses that service the hospitality space and then accelerates their growth by selling their offerings into AHT and BHR's 130+ hotels. For example, in November 2017, AINC acquired an 85% stake in J&S Audio Visual, a company that provides audio and visual equipment to hotels and convention centers, for $26 million. Since the acquisition, J&S's revenue and EBITDA have increased by 22% and 55%, respectively, bringing the effective purchase multiple from 7x down to 4x in a very short period.

- The company has agreed to help fund new property acquisitions by AHT and eventually will with BHR as well. Management recently formalized the relationship and developed a program called Enhanced Return Funding Program, or ERFP, together with AHT. As part of the ERFP, AINC has agreed to fund up to 10% of the purchase price on AHT's new hotel acquisitions in the form of capital improvements to AHT's properties, effectively reducing AHT's down payment on a typical new hotel from 30% to 20% of the purchase price, while also increasing AHT's returns on the acquisition. Once that new hotel is in the AHT portfolio, AINC begins providing asset management, project management and other ancillary services to that hotel, potentially generating >50% year one cash-on-cash returns for AINC on the expenditures that it helped fund. I expect AINC will replicate this ERFP program with BHR over time as well.

- AINC is evaluating launching new investment platforms that it would manage and that would generate additional base and incentive fees for the company – for example, a mezzanine fund or a new select service hotel REIT.

In short, the company has proven that is has many paths to accretive growth. Given this attractive growth outlook, it should be surprising that AINC is currently valued by the market for ~8x EBITDA and <10x adjusted EPS. So, why does this opportunity exist? Besides the fact that hotel companies have fallen out of favor with investors, the market does not trust Monty Bennett or AINC's corporate governance.

In August of this year, AINC acquired Remington Project Management from Monty Bennett, its Chairman and CEO, for 12.5x EBITDA. This business manages capital projects for hotels including ground-up development, renovations, conversion and maintenance work. Importantly, Monty took his payment for Remington in the form of AINC convertible preferred stock, which significantly increased his exposure to AINC's prospects. After this transaction, Monty has the following exposures to each of the three affiliated public entities: $40 million at AHT, $20 million at BHR and $240 million at AINC. Given these weightings, I believe that Monty's substantial stake in AINC relative to the REITs ensures that investors in AINC are well aligned with that of management.

The stock declined 40% following the announcement of the deal, and it was around this time that the Fund chose to initiate its position. After the deal was digested and the stock recovered almost the entire loss, the company initiated an unexpected equity offering without clearly communicating the use of proceeds, causing the stock to sell off by ~25%.

Recently, the company has suggested that they could eventually try to acquire another entity owned by Monty – Remington Property Management. I believe that if this transaction were to be pursued, it would be under similar terms to the Remington Project Management business. The benefits of such a deal, if it were to happen, would be that i) it would likely be the last related party acquisition since Monty would have no other independent hotel businesses outside of the three public entities (which should alleviate any concerns over future transactions) and ii) it would further increase the amount of fees that AINC generates from each property that the REITs own, and as such would grow even more accretively every time the REITs acquired a new property.

I believe that at <10x earnings, with a credible path to significant earnings growth, AINC offers a compelling value proposition and has many of the characteristics that I look for in prospective investments. While I understand the market's concern regarding governance, I take comfort in the CEO's significant investment in AINC, the fact that related party transactions may soon be in the rear-view mirror and lastly, that the worst case already seems to be priced into the current valuation ascribed to the company by the market.

Outlook

Earlier this month, Federal Reserve Chairman Jay Powell said that the central bank is "a long way" from getting rates to their natural level, which the market took as a signal that more rate hikes are coming. It is clear that this Fed wants to prevent the economy from overheating and get rates to a higher level so that they can again lower them to stimulate the economy in the next recession.

In the following week, the Treasury auctioned 10-year notes which required the highest auction yield since 2011 at 3.2%, up from 2.4% at the start of this year, suggesting that demand for global fixed income is weakening at a time when the US budget deficit is expected to approach $1 trillion in 2019, up from <$500 billion in 2015[5].

At the same time, the spread between the 10-year and 2-year treasuries, which has historically narrowed when investors expect lower future growth or a recession has narrowed to less than 30 basis points from a 2010 high of almost 3%[6].

These diverging data points, the Fed implying they think inflation and growth are a real risk to the economy, while bond market implying that a recession or slowdown are on the horizon, have led to increased market volatility as investors digest the impact of increasing interest rates on both the economy as well as asset prices.

To date, the stock and bond markets seem to suggest that the risk of recession in the US has recently increased. Cyclical stocks, such as those with exposure to housing and auto end markets, have sold off sharply recently despite macro datapoints pointing to a strong economy.

With that said, corporate earnings, consumer and business confidence, and personal and corporate balance sheets all appear to be in good shape while the S&P 500 Index is trading at a reasonable ~15x[7] forward earnings multiple. As I said in last quarter's letter, I have generally found that the companies I am doing diligence on see a favorable economic backdrop.

I continue to think that it is prudent to retain dry power that can be deployed when periods of significant market and/or economic volatility surface. You can be assured that I have used the recent selloff in stocks

[5] Source: https://www.thestreet.com/markets/u-s-10-year-bond-auction-draws-highest-yield-since-2011-overall-demand-wanes-14740859
[6] Source: Bloomberg
[7] Ibid.

to add to many of the Fund's positions and that the portfolio consists of defensive stocks with predictable and growing earnings streams that trade for reasonable valuations and have strong balance sheets.

The Fund remains well positioned to take advantage of any additional opportunities that would be created should the recent selloff continue.

<u>Monthly Performance Summary</u>[8]

2018	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
1 Main Capital Partners - Gross		-0.8%	1.4%	-0.5%	6.7%	0.4%	3.2%	4.8%	-2.9%				12.7%
1 Main Capital Partners - Net		-0.9%	1.3%	-0.6%	6.3%	0.2%	2.4%	3.7%	-2.4%				10.1%
S&P 500 index - incl dividends		-3.6%	-2.5%	0.4%	2.4%	0.6%	3.7%	3.3%	0.6%				4.6%
Russell 2000 - incl dividends		-4.2%	1.3%	0.9%	6.1%	0.7%	1.7%	4.3%	-2.4%				8.3%

Thank you for your continued support and confidence. Please reach out with any questions at yaron@1maincapital.com or 305-710-8509.

Sincerely,

Yaron Naymark

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