VOSS CAPITAL

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Dear Partners,

In Q2 2017 the Voss Value Fund returned -0.14% to investors net of fees and expenses, compared to a 3.1% total return for the S&P 500 and 2.5% for the Russell 2000.

Voss Value Fund, LP

ESTIMATED NET MONTHLY PERFORMANCE | 2017			
PERIOD	VVF (Net)	VVF (Gross)	S&P 500 TR
JANUARY	0.12%	0.23%	1.90%
FEBRUARY	3.14%	4.01%	3.97%
MARCH	0.38%	0.56%	0.12%
1st QUARTER	3.66%	4.83%	6.07%
APRIL	0.39%	0.57%	1.03%
MAY	-2.01%	-2.41%	1.41%
JUNE	1.50%	1.96%	0.62%
2nd QUARTER	-0.14%	0.07%	3.09%
JULY			
AUGUST			
SEPTEMBER			
3rd QUARTER	0.00%	0.00%	0.00%
OCTOBER			
NOVEMBER			
DECEMBER			
4th QUARTER	0.00%	0.00%	0.00%
YEAR TO DATE	3.51%	4.90%	9.34%

The table below shows the Voss Value Fund's Net Returns compared to some of the relevant indices over various timeframes:

Return Comparison as of June 30th 2017					CAGR		
	1 Month	3 Month	YTD	1-Year	3-Year	5-Year	ITD
Voss	**1.5%**	**-0.2%**	**3.5%**	**20.0%**	**13.3%**	**18.4%**	**18.2%**
S&P 500	0.6%	3.1%	9.3%	17.9%	9.6%	14.6%	16.6%
Russell 2000	3.5%	2.5%	5.0%	24.6%	7.4%	13.7%	16.3%
Russell 2000 Growth	3.4%	4.4%	10.0%	24.4%	7.6%	14.0%	16.5%
Russell 2000 Value	3.5%	0.7%	0.5%	24.9%	7.0%	13.4%	16.0%
Credit Suisse L/S Index	-0.2%	3.1%	6.6%	8.4%	3.0%	7.0%	7.9%
Credit Suisse HF Index	-0.5%	0.8%	2.8%	5.8%	1.5%	4.5%	5.1%

All YTD performance figures are unaudited, estimated, and may be subject to subsequent adjustment. A limited partner's actual returns may vary from published fund returns based on the timing of capital and fee arrangements. This statement represents information based on the policies of the fund's managers and general partner. Please contact Travis Cocke, Managing Partner of Voss Capital, LLC, with any inquiries.

Mr. Market continues to be riddled with befuddling contradictions and characterized by abnormal polarization. In late June, the correlation between the Nasdaq and Russell 2000 broke down and went negative with capital toggling violently back and forth like a shuttlecock between value and momentum stocks. Lately, this has consisted of small cap underperformers becoming a source of capital to chase larger stocks with price momentum and high projected revenue growth. State Street Global Advisors has called the current environment "the longest period of underperformance for value since the late 1940s."[1] The return spread between the Nasdaq and Russell 2000 Value index had blown out to >21% recently, the second highest rolling six month spread (behind the peak of the internet bubble) since the early 1990's.

Year to date through June 30th, the Russell 2000 Value index was +0.5%, while the S&P 500 was up 9.3% and the Nasdaq Composite was up 14.1%. While our performance relative to the latter two indices is disappointing, we are still soundly outperforming the smaller value stock indices with lower net exposure and while holding much cheaper stocks that have better return prospects than the market as a whole.

The forward P/E multiple on the Russell 2000 is ~18.6x, which is in the 94th percentile of its history. The median stock valuation by a variety of metrics is in the 99th - 100th percentile.[2] Thus the breadth of high valuation is currently the greatest in history and by a large magnitude. On the positive side of the ledger, corporate profit growth has been strong, buoyed by deflationary raw materials inputs and rather strong consumer balance sheets. The percentage of S&P 500 constituents beating analysts' sales and earnings expectations is at a 13-year high.[3] Reported EPS growth for the S&P 500 in Q2 clocked in at 11%, with 10 of the 11 sectors showing positive growth (only Utilities did not).[4] Within the S&P 500, sector performance YTD is all over the map, ranging from -10.4% for Energy and +22.3% for Technology. There is even wider sector return dispersion for small caps (see table below).

Given the sector weightings of the Russell 2000 Value index, the value trade in part comes down to a large sector bet on financials (~30% of the index). Conversely, the Russell 2000 Growth index is dominated by technology and healthcare stocks. We have our fair share of financials exposure, but no energy exposure.

Russell Global Sectors	Russell 2000 Value Weight	Russell 2000 Growth Weight	YTD Return
Consumer Discretionary	11.2%	15.7%	3.2%
Consumer Staples	2.4%	2.3%	-4.9%
Energy	6.0%	1.0%	-25.7%
Financial Services	29.6%	7.6%	-0.7%
Health Care	5.4%	24.3%	20.0%
Materials	5.9%	8.2%	3.5%
Producer Durables	11.1%	15.8%	5.4%
REITs	12.7%	3.1%	6.4%
Technology	8.4%	19.6%	13.6%
Utilities	7.2%	2.4%	10.2%

Some of the increase in our financial sector exposure, aside from the retail REIT basket detailed in our last quarterly letter, has come from a recently purchased basket of three regional bank stocks. These three are Franklin Financial Network (FSB), Bank of Internet (BOFI), and Customers Bancorp (CUBI). Thematically, these banks are all branch-lite and efficient, something the market curiously seems to be discounting if the company is an actual bank, but bidding valuation up aggressively on if labeled as "fin-tech" (see Square or Paypal).

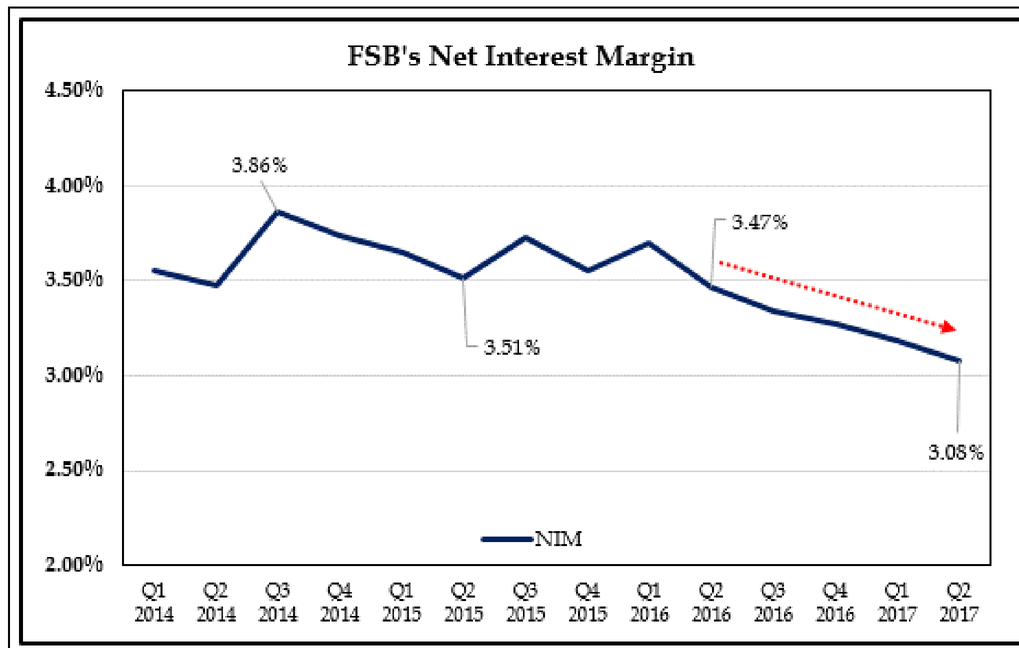
Franklin Financial Network (FSB)

Franklin Financial is a branch-lite bank with an experienced management team, pure-play exposure to the thriving Nashville MSA, and ample runway to grow loans, earnings, and book value per share at 18-20% p.a. the next few years. After reporting earnings last week, the stock has traded down to 1.3x our 2018 tangible book value estimate and 11x earnings, a 40% discount to its peer group, despite having superior growth, credit quality, and returns compared to the peers. We believe several things spooked growth oriented investors in the latest quarter, but most of these negatives or perceived negatives will abate over the

next few quarters, when in conjunction with a potential hard catalyst before year end creates a compelling entry point in the low-$30s.

The negatives include substantial net interest margin compression (NIM) over the last year, a slower than expected improvement in the bank's efficiency ratio and a sequential slowdown in loan growth to 12.5% from the previous 25%+ rate. Additionally, EPS growth was negative due to a large secondary offering in late 2016 that diluted share count.

FSB focuses on real estate and construction lending primarily in Williamson County in Tennessee (the 15th wealthiest county in the country, with median household income above $100,000), with about 79% of the total loan portfolio designated as "real estate." The housing market in the Nashville area is very strong with Freddie Mac deeming it the healthiest housing market in the country. In July, the median home price was up >10% year-over-year and finished housing inventory tight at only ~1.5 months of supply at the current sales pace (average days a listed home is on market is 25). Within real estate, FSB's loans run the gamut from Construction, Commercial Real Estate (CRE), and Residential at 25%, 28%, and 23% of the total loan portfolio, respectively. The remainder of the loan book is Commercial and Industrial, with a growing Healthcare vertical at ~10% of total loans, and "non-healthcare" around 13% of loans. They have very limited consumer exposure. The healthcare underwriting team was poached from a different Tennessee bank and it is a new vertical for FSB as they tried to quickly diversify away from real estate to appease regulators. Ironically, the larger loan sizes and loan concentration that comprises the healthcare book is one area we flag as a risk and will keep a watchful eye on.



As shown in the chart above, FSB's NIM has compressed with headwinds coming from a variety of factors, including a shift in asset mix towards lower yield securities immediately after the November 2016 equity offering, rising Government Deposits as a percentage of total deposits (raising cost of deposits), and a shift to lower risk, lower yielding owner occupied real estate loans. FSB had handled Williamson County municipal deposits for many years but recently added Rutherford County in late 2016. These deposits, which are collateralized by securities, peak in early March and trough in September. They are very profitable, but act as a NIM suppressant and we believe the sell side was caught off guard by its impacts (one sell side downgraded the stock on "NIM compression" before the latest conference call even occurred). There will be a sharp seasonal drawdown in Government deposits that will boost NIM in the back half of the year, which we believe will make the optics of the company improve as we believe this dynamic is not well known. The company will also get NIM tailwinds as they continue to convert their equity proceeds into loans and will be reloading the balance sheet with higher yielding construction loans.

FSB has spent the last twelve months spending aggressively on internal control technology to satisfy banking regulators, who issued an MOU (Memorandum of Understanding) that essentially forced them to slow down their Commercial Real Estate

(CRE) loan growth and restricted their ability to make any acquisitions. We believe this has been a major distraction for management (as well as another NIM compressor as CRE loans have above average yields) and they have been working extraordinarily hard to make sure the upcoming regulatory exam goes well. We believe by mid-Q4 it will be apparent how the exam went and the "tell" would be them announcing the closing of their pending acquisition of Civic Bank & Trust that was put on hold until they were deemed worthy by the regulators. The acquisition going through will indicate that the company is back in good graces with regulators and can kick-start more low cost deposit oriented acquisitions and will act as a hard catalyst to flip investor sentiment from "wait and see" mode to emphatically positive, leading to multiple expansion on a quickly growing earnings stream. Lastly, FSB's management team has a long history of building out high growth middle-Tennessee focused banks and eventually selling them at premium valuations. We think this iteration will be end no differently, as the bank offers pure play leadership in a burgeoning metropolitan area

Bank of Internet (BOFI)

BOFI, like FSB, is a well above average bank as measured by growth, returns, profitability, and credit quality and trades at a substantial discount to trading comps. What drew our attention to BOFI was seeing the above average metrics and steep valuation discount in conjunction with dozens of short seller write-ups and 56% of the effective float shorted. BOFI is a branchless bank that has been able to grow deposits at a mid-30s percent CAGR for the last six years as internet banking gains widespread acceptance and they are able to pay slightly more for deposits as their overall cost structure is lower with no physical footprint. 78% of BOFI's loan book is comprised of single-family and multi-family housing with a conservative 58% median loan-to-value ratio at the time of underwriting and a concentration in southern California. They have a nice niche lending to high net worth borrowers who have strong balance sheets but funky income situations and tax returns, such as many entrepreneurs or those reliant on capital gains/partnership income. With the passage of over three years from the initial public short reports, almost every short thesis point has been systematically debunked, such as the allegations of inflated appraisal values or fears of major NIM compression. Management has corrected the course in this regard, by repositioning the loan book to become a beneficiary of rising interest rates and sidestepping interest rate risk that was feared. The company also has a unique and growing relationship with H&R Block, whereby they handle (quite profitably) several online tax related products like refund advances, refund transfers, and IRA accounts. We believe fatigued shorts will slowly capitulate and the stock will revert to closer to 2.5x tangible book value per share, providing 58% upside from our $23.60 cost basis.

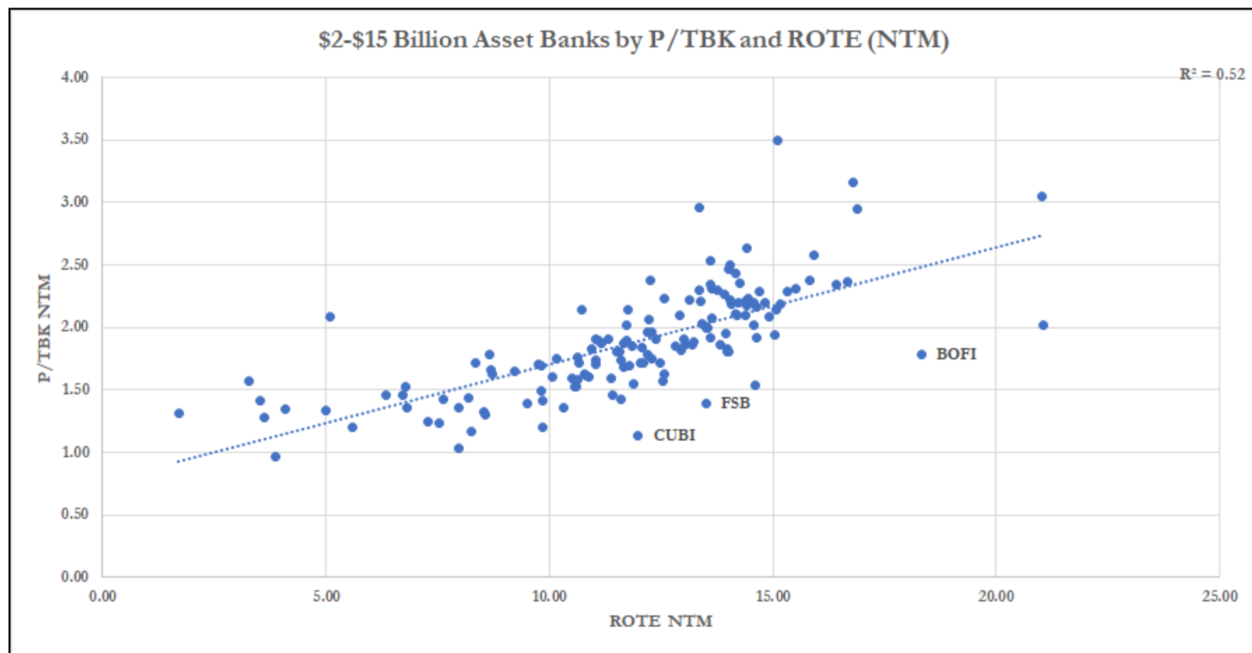
Customers Bancorp (CUBI)

The final bank that is part of our branch-lite trio is Customers Bancorp (CUBI). CUBI is the cheapest of the group at 1.1x our 2018 estimate of tangible book value and 10x earnings, has a superior efficiency ratio (~40%), an improving deposit profile, and accelerating earnings growth. It is led by longtime bank veteran Jay Sidhu, who managed Sovereign Bank for 20 years grew it from $12 million to $12 billion in market cap over a 20 year period.

The idiosyncratic aspect of CUBI is BankMobile, an online only banking enterprise asset that generates almost all its income from debit interchange fees. As CUBI approached $10 billion in assets, they determined divesting BankMobile was prudent as tripping the $10 billion asset threshold limited the interchange revenue they could capture, per regulations of the Durbin Amendment.

The stock sold off hard when a deal they had for BankMobile fell through, but management has indicated they are once again close to consummating a deal and are confident they will sell BankMobile for "well in excess of $100 million." This will give CUBI a nice one-time boost to book value, provide an earnings tailwind, and will make the CUBI story simpler. While the stock has languished, we believe it could re-rate it to 1.5x tangible book and the 15x earnings range over the next few quarters post BankMobile divestiture and when the company shows it can grow earnings consistently in the 15% range.

When plotting these three banks against the entire trading comp universe, despite a superior financial profile, you can see how much of an outlier each one's valuation based on what we believe what is one of the most important and highly correlated metrics, return on tangible equity.

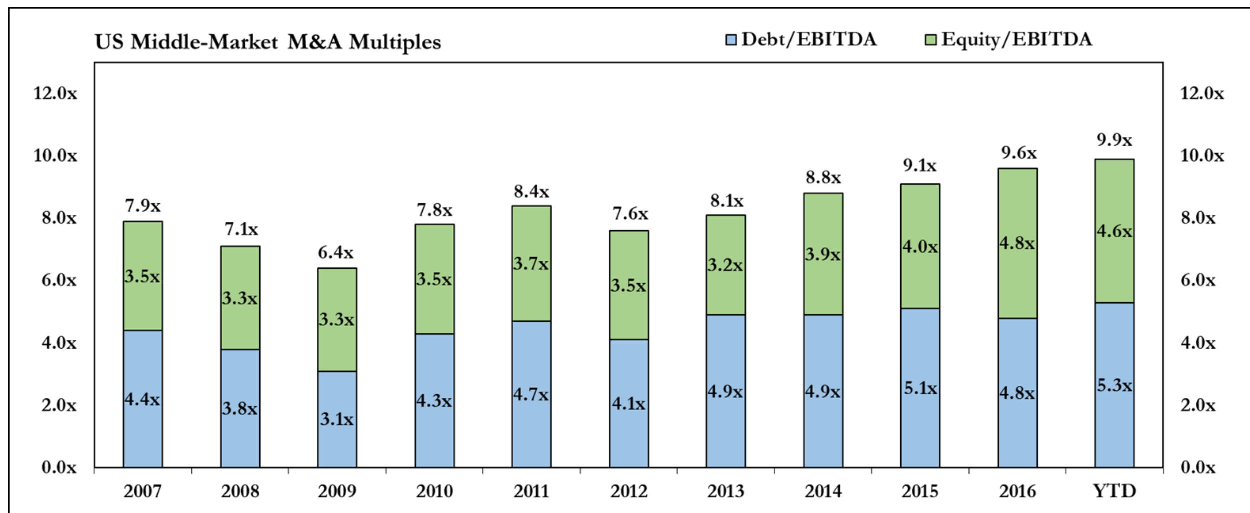


While we are still finding pockets of value and stocks with idiosyncratic catalysts, such as these few banks, we believe overall that equities pricing remains very inefficient this late in a bull market. The fundamental minutiae are becoming less important for most stocks. As economics research has repeatedly proven, an auction is not an efficient pricing mechanism, as participants tend to overpay in aggregate. Auction participants especially overpay for things whose valuation is hard to determine, and systematically overpay if they are novices. With a flood of capital coming in from first time, low information Millenial investors, they will tend to bid up prices on companies whose valuation is abstract (e.g. money losing tech firms or pre-clinical biotechs), yet ultimately have a high probability of being worthless or settling 50-90% lower. Charles Schwab reported that in Q2 new retail account openings were up 50% year-over-year, up to levels not seen since the peak of the internet bubble.. The fact that stocks with deteriorating fundamentals that are impossibly overhyped remain aloft against the stubborn gravity of hundreds of years of economic reality speaks to investors' incalculably limitless credulity in the face of the social proof offered by a rising price. It also speaks to the fact that fundamentals are consistently trumped by share float dynamics and technical supply/demand in the short to intermediate term, something we are emphasizing in our process more and more. In addition to the high conviction, yet low information traders crowding out prudent fundamentally driven capital, we believe high valuation M&A will tick up. Management teams are starting to lever up more to pay all-time high valuations at peak margins for acquisitions (or their own shares) and citing ambiguous strategic rationale of cost synergies forecasted some 2-3 years out. Some other traditional sources of fundamentally driven capital have also slowly capitulated on their discipline and are chasing performance (e.g. Walmart is on an eCommerce buying binge, Apple has invested $1 billion in Softbank's $93b "Vision Fund" which has questionable valuation discipline). These sources collectively have deep enough pockets to sustain elevated valuations for quite some time longer.

In attempting to evaluate aggregate net equity supply/demand, the balance tips highly in favor to the demand side of the scale. We estimate that YTD through the end of June in the US markets, share buybacks plus cash-based M&A (e.g. excludes share based M&A to gauge removal of shares/reduction of equity supply), exceeds equity issuance in IPOs and follow-on offerings by at least a 2.5:1 ratio, with a much higher ratio globally.[5] The IPO backlog also remains quite low and is only a tiny fraction of executed buybacks.

Furthermore, the private equity fund raising bonanza continues unabated, which could ultimately lead to an uptick in small cap M&A despite record high valuations for deals (shown below), and thus provide further incremental reduction of equity supply.

In Q2, private equity accounted for ~30% of total corporate M&A, a proportion that is slowly ticking up over the last few years.[6] Private Equity has in excess of $750 billion of dry powder, about $100 billion of which is reaching the end of its investable timeframe. The total dry powder will likely be levered into >$1.5 trillion of buying power based on prevailing deal structures.



Source: Pitchbook

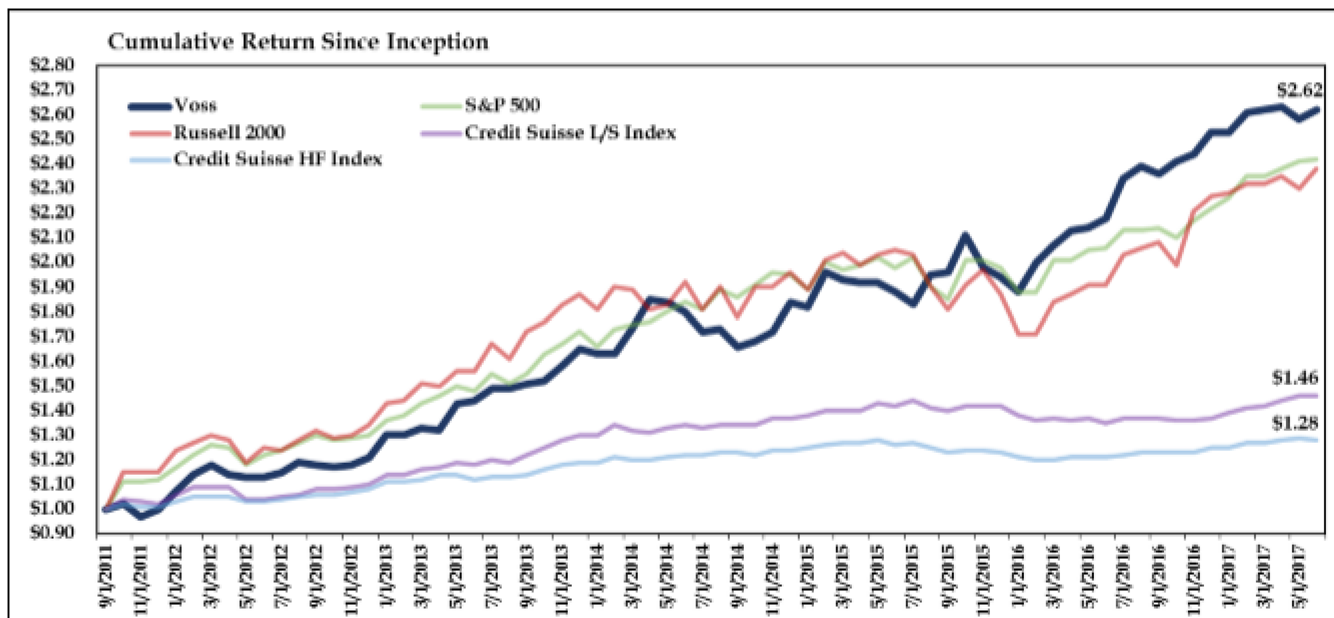
The Voss investment methodology is about valuation discipline, self-control and risk control. We can't judge our own long-term progress nor get distracted from our discipline based on how a few speculators are doing over a few short months. For us to improve on a relative basis, money doesn't have to enter or leave equities, it just has re-position and rotate into value and out of overvalued companies with deteriorating fundamentals, instead of vice-versa. We also need to stop absorbing many small losses on the short side, where it has felt like we've been stuck in a one-step-forward, one-step-backwards tiresome tango for months on end, unable to find our rhythm. If the present trend of smaller cap value lagging this badly continues, it is a near certainty we will underperform on a relative basis, as we will keep gingerly tiptoeing around the banana peels the market so blithely tosses in our path. However, we feel many factors can play into small cap value's favor soon once again, such as the potential for corporate tax cuts, private equity dry powder, and simple mean reversion. Given the rampant dichotomies in the market, we still find the opportunity set large for a long/short investor. As usual, exploiting the opportunity set will require patience as mean reversion has certainly not been happening in any reasonable timeframe, nor is it subject to any immutable rules requiring it to turn in our favor.

In his novel, *My Name is Red*, Orhan Pamuk tells the story of old Persian miniaturists who had drawn the same horse with the same passion for 50 years, memorizing each stroke such that they could re-create the tiny horse painting even with their eyes closed. In the hopes of continual improvement that leads to consistently delivering uncorrelated alpha to our Partners, we patiently and stubbornly devote ourselves to our craft in the same way--but we do so with our eyes wide open.

To Continued Alpha,

Voss

1: https://www.wsj.com/articles/hot-stock-rally-tests-the-patience-of-a-choosy-lot-value-investors-1502020804
2: Source: Goldman Sachs Research
3: Source: Bank of America Merrill Lynch report, August 7th, 2017: US Equity Strategy Recap
4: Source: FactSet
5: Sources for M&A, IPO, Equity Offering data compiled from Bloomberg, Factset, and Goldman Sachs.
6: Source: Pitchbook



Voss Value Fund Monthly Net Returns Since Inception

	Jan.	Feb.	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.	Year
2011										1.51%	-4.09%	3.17%	**0.44%**
2012	7.04%	5.72%	3.90%	-3.44%	-1.13%	-0.21%	2.26%	3.04%	-0.07%	-1.49%	1.17%	2.68%	**20.87%**
2013	7.22%	-0.18%	2.18%	-0.63%	8.80%	0.29%	3.32%	0.02%	1.55%	0.70%	3.87%	4.64%	**36.21%**
2014	-1.24%	-0.16%	6.16%	6.70%	-0.20%	-2.20%	-4.47%	0.43%	-3.82%	0.94%	2.69%	6.69%	**11.25%**
2015	-1.21%	7.65%	-1.15%	-0.49%	-0.12%	-1.91%	-2.80%	6.66%	0.22%	7.72%	-5.97%	-1.87%	**5.69%**
2016	-3.24%	6.48%	3.43%	2.59%	0.90%	1.84%	7.26%	1.86%	-1.12%	2.22%	1.21%	3.72%	**30.23%**
2017	0.12%	3.14%	0.38%	0.39%	-2.01%	1.50%							**3.51%**

Top 3 Market Drawdowns Since Voss Inception

			Performance		Voss Relative		Correlation	Historical
Peak	Trough	Index	Index	Voss	Performance	Length (Days)	During Period	Correlation
6/24/2015	2/11/2016	Russell 2000	-26.4%	-2.3%	+24.1%	161	0.22	0.42
5/22/2015	2/11/2016	S&P 500	-14.2%	-2.8%	+11.4%	183	0.18	0.39
3/5/2014	10/13/2014	Russell 2000	-13.2%	-5.5%	+7.7%	155	0.17	0.42

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