VOSS CAPITAL

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Dear Partners,

In Q4 2017 the Voss Value Fund returned -1.26% to investors net of fees and expenses, compared to a 3.3% total return for the Russell 2000 and a 6.6% total return for the S&P 500. The Fund's total gross exposure stands at 128.5% and the beta-adjusted net long exposure is 51%. Our top 10 longs have a 59.0% weighting and our top 10 shorts have a gross weight of -9.5%.

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	0.31%	0.47%	2.06%
AUGUST	0.61%	0.84%	0.31%
SEPTEMBER	2.63%	3.34%	2.06%
3rd QUARTER	**3.58%**	**4.69%**	**4.48%**
OCTOBER	-0.27%	-0.25%	2.33%
NOVEMBER	-3.40%	-4.11%	3.07%
DECEMBER	2.50%	3.19%	1.11%
4th QUARTER	**-1.26%**	**-1.29%**	**6.64%**
YEAR TO DATE	**5.87%**	**8.41%**	**21.83%**

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

Net Return Comparison as of December 31st, 2017					CAGR		
	1 Month	3 Month	YTD	1-Year	3-Year	5-Year	ITD
Voss Value Fund, LP	**2.5%**	**-1.2%**	**5.9%**	**5.9%**	**13.4%**	**17.2%**	**17.1%**
S&P 500	1.1%	6.6%	21.8%	21.8%	11.4%	15.8%	17.2%
Russell 2000	-0.4%	3.3%	14.6%	14.6%	10.0%	14.1%	16.5%
Russell 2000 Growth	0.1%	4.6%	22.2%	22.2%	10.3%	15.2%	17.0%
Russell 2000 Value	-1.0%	2.0%	7.8%	7.8%	9.5%	13.0%	16.0%
Credit Suisse L/S Index	0.8%	3.3%	13.4%	13.4%	4.3%	7.1%	7.3%
Credit Suisse HF Index	0.9%	2.3%	7.1%	7.1%	2.5%	4.2%	4.7%

In mid-October, just as we pulled within spitting distance of the S&P 500, Murphy's Law intervened and The Great Humiliator assumed the proportions of a more than worthy adversary. This past year we did not live up to the standards we are trying to achieve and are far from content with our returns lately. Why did we underperform? As with much in life, the truth is neither pure nor simple, and our underperformance is due to a variety of reasons. At times during the year, we held a lot of cash and ran low net exposure (averaging 61.4% on the year); our shorts detracted several percentage points on the year; our retail REIT basket was a major performance drag; we had some self-inflicted trading errors due to lack of patience entering some shorts with tight floats; and our largest long was flat all year (Quorum). Furthermore, relative style and factor performance was the inverse of 2016, with Small Caps underperforming Large Caps and "Value" stocks underperforming "Growth" stocks by a wide margin (evidenced by the Russell 2000 Value Index being up 7.8% in 2017 versus the S&P 500's 21.8%). We've avoided any style drift and thus have been fighting the current preferences of the market. History shows, and we believe that, ultimately these style factors will balance out and after several years of substantial underperformance for smaller value names (outside of 2016), any mean reversion in favor of small cap value would once again give us a tailwind.

38 of 39 global asset classes that Deutsche Bank monitors had positive returns in 2017. Only corn was negative, ending the year down a paltry 0.4%. The S&P had positive returns in every month, the first time in its storied history. 2017 was the least volatile year in history by a variety of measures. However, as usual, watching the magnitude of moves in some small cap stocks would spoil the rich illusion of peaceful harmony of the market offered by a casual following of the NASDAQ or S&P 500 indices. After a record long period without a 5% or even a 3% correction, finally, in nine short trading days this year, the S&P 500 fell sharply crossing the -10% "correction" threshold.

To be sure, a strong global economic backdrop and briskly growing corporate earnings have provided some fundamental underpinning to the market's rise. However, the dispersion of returns and unequal proportion of rewards has been puzzling.

For many companies, missing estimates across the board (top and bottom line) and significantly lowering forward earnings/revenue guidance is not resulting in negative market consequences. Some previous historical cause and effect relationships seem to no longer apply as ETF and retail fund flows often overwhelm and out-gun fundamentally driven investors. We must practice unbuckling our minds from linear thought and the familiar bounds of history: we have to explicitly consider previously unfathomable outcomes and valuation ranges, including those that are unprecedented. One does not need to look hard to find companies that have consistently lost money for 10 to 15 or more years running and will likely never even recoup their cumulative cash burn, thus never providing a satisfactory return on invested capital. It is almost as if the market has forsaken fundamental forces of capitalism, and instead many pockets of it have come to resemble a "crowd-sourced funding" platform (e.g. Kickstarter), whereby people indefinitely give cheap funds to companies they like without regard for future profitability or valuation. This mentality of many market participants can be simplified to "XYZ is fully priced, but I think it will become more so." Because of this pervasive mindset, market momentum has overtaken any notion of value, and despite the recent sharp correction, this mentality may linger until there is a more thorough washout. Even in this early February dip, almost none of our shorts have come remotely close to our base case valuations or price targets and in aggregate still have substantial downside. While the willing disbelief of people can last for a long time and it does seem that old analytical rules might no longer apply, we believe ultimately that cash flow will matter once again and that values and prices in the public market will inevitably converge.

Levered Cyclical Industrial Shorts

Given we are nine years into an economic expansion, the cyclical character of all that surrounds us hasn't been seen in so long that it is all but forgotten and unrecognizable. For this reason, we are finding many attractive shorts within the cyclical industrials space. We are combing through companies at all-time high margins, all-time high valuations (by a wide degree), all-time high leverage, and all-time low short interest in order to comprise a group of shorts. In a recessionary environment, these are companies that may experience both significant revenue and profit declines due to their inherent operating leverage.

One such example is Sun Hydraulics (SNHY). SNHY is a manufacturer for the hydraulics market and rugged electronic controls, displays and instrumentation for recreational and off-highway vehicles. The company acquired the bulk of the electronic display segment, via Enovation Controls in December 2016, and admits the two segments have little synergies between them. This was not a bad acquisition as they paid 9.5x EBITDA, and it is showing tremendous growth, however we think its main end markets of recreational vehicles and boats will prove to be wildly cyclical, as most discretionary, large ticket consumer purchases are. Using the Fed's "Pleasure Vehicles Index" (consumer spending on boats, aircraft, and ATVs) as a proxy for their demand drivers, we can see that spending on vehicles in this category declined by 39% in the last recession. The Enovation Controls acquisition has also dramatically worsened the company's inventory turnover and working capital dynamics. The hydraulics segment's largest end market demand driver is construction equipment, particularly equipment that is used in commercial and multi-family development (e.g. 3-5 story structures). Using order and shipment data from the National Fluid Power Association, we can see that business is doing quite well after coming out of a slight slowdown in 2015. This segment also revealed its true cyclical character in 2009 with a 58% year-over-year revenue decline in the heart of the recession.

At the company's Analyst Day in September, SNHY revealed their "2025 Vision" which included targeting $1 billion in total revenue with 24% EBITDA margins. Their goal is to double the revenue of both segments organically, which implies an 8-9% CAGR over the next seven years. This target requires a large acceleration compared to their 6% revenue CAGR achieved from 2005-2015. Doubling the revenue of the existing business, however, would only get them to $620 million, well short of their stated $1 billion target. In order to achieve this objective they would need to acquire an additional $350+ million in sales, which would come from 3-5 acquisitions of companies with sales bases of between $50 and $100 million. At a cost basis of $67.37 for our short, the company was already priced at an Enterprise Value of >8x their aggressive 2025 EBITDA targets. Compare this to the 15-year median NTM EV/EBITDA multiple of 11x as a benchmark. We initiated the short thinking the asymmetry was skewed heavily to the downside. The shares were pricing in acceleration of uninterrupted growth over the next seven years, and they have substantial execution risk due to the need/stated desire to acquire revenue in excess of the entire current base, which is also already fully priced in. If there is a cyclical slowdown or recession along with some multiple compression, the shares still have a long way to fall.

<u>Update on Retail REITs</u>

While it is said that life "favors the specific and punishes vague requests," the market paradoxically does the opposite when in a festive mood. Research shows time and time again that the more bidders there are competing for an object (or asset), with each having roughly the same information, and the more uncertain its value is, the more likely everyone is to systematically overpay (think Beanie Baby auctions on eBay in 1999). For us, the less information we have compared to other "bidders" or the more uncertain we are about the underlying asset value, the lower we are apt to bid or, more importantly, we will avoid bidding altogether.

On the contrary, one area of the market we find to be easier to pin down a more precise valuation due to good disclosures and the liquidity and high frequency of comparable transactions in the private market, is that of REITs. We previously highlighted CBL as a favorite within retail REITs. However, when we saw weakening re-leasing spreads a few quarters ago from peer WPG, management's lack of urgency, and further relative value compression of other higher quality retail REITs, we changed our minds and swapped into a few others, namely Kimco Realty (KIM), Kite Realty (KRG) and Tanger Factory Outlets (SKT).

Tanger's outlet store format provides retailers the lowest cost of occupancy (rent per square foot relative to their store sales per square foot) and has proven there is resilient demand for its space, year-in and year-out, as it has never ended a year with occupancy below 95% and consistently demonstrates positive re-leasing spreads, including throughout the Great Recession. SKT also has a cleaner balance sheet than CBL with limited near-term debt maturities, no department store exposure, and thus less capital expenditure requirements that come from redeveloping large anchor boxes.

With Kimco and Kite Realty, our thinking is that high-quality grocery-anchored shopping centers have limited existential risk as compared to enclosed B-class malls, better balance sheets, and more liquid real estate/credit markets. This is evidenced by 10+ bidders every time they are putting their worst quality properties up for sale while fetching cap rates well below their overall implied cap rate. Private market transactions for comparable properties continue to show the public retail REITs trade at substantial discounts to liquidation value, with some having 80%+ upside to reach consensus Net Asset Value that is based on private market cap rates.

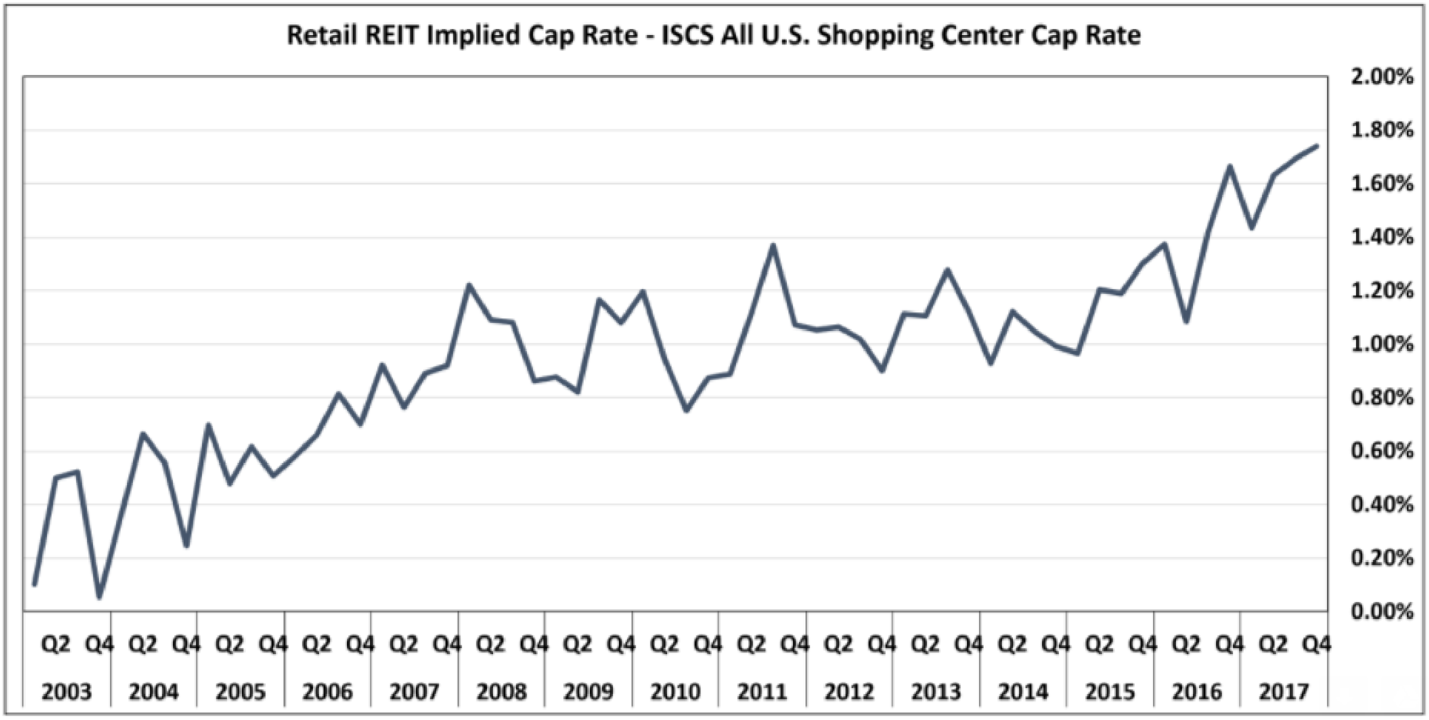
While we have been unfortunately early and have endured mark-to-market losses on the names, we have recently been buying more KIM and KRG at implied cap rates in excess of 8.5% and 9%, respectively. These two REITs in particular get a substantial amount of their NOI from long term ground leases to large retailers such as Walmart, Lowe's and Home Depot. All NOI is not created equal, as these ground leases would sell at very high valuations (low cap rates), further underpinning the NAV and exacerbating their discounts to private market value. Another point of distinction is that KIM gets ~12.5% of its annualized base rents from the NYC metro area, and the private market sales for shopping centers in the metro area continue to transact at 4-caps, on average[1]. As opposed to showing negative re-leasing and new leasing spreads like the lower quality mall REITs, KIM and KRG continue to show highly positive rent spreads and have significant opportunity to further boost their average rents as legacy tenants (e.g. K-Mart) with leases well below current market rents are booted and replaced with new tenants paying higher rates, in some case up to 300%+ higher. With each of these REITs having at least 85% of their debt at fixed rates (98% fixed rate for KIM and 92% for KRG) and average debt maturities extending by five to ten years or more, they have little balance sheet exposure to rising rates in the near term.

Using history as a guide and evaluating interest rates relative to commercial real estate's cap rates or public REIT dividend and FFO yields, we think the market is currently overly punishing the REITs for rising interest rates, and our names have already priced in a much more dramatic rise in rates that may or may not be forthcoming. If inflation picks up, they could also benefit from being able to push through higher rents while having fixed debt service costs.

As shown above, from the middle of 2012 to early 2014, the 10-year treasury yield rose in similar timeframe and magnitude (from 1.5% to 3.0%) as it has from Q2 2016. At the time there was no panic in the REITs.

	KIM	KRG	SKT
15-Year Median	1.55%	1.90%	0.77%
Current	5.17%	5.93%	3.45%

This table above shows the historical median spread in dividend yields over the 10-year treasury yield. Give these three REITs' spreads have blown out to several percentage points wide relative to their 15-year median (which includes the 2008 crash), we believe that the equities have already priced in interest rates of up to 300 basis points higher.



As further evidence of the public/private disconnect, the chart above shows the spread between the implied cap rate of a Retail REIT basket versus actual aggregated private market transaction data from the International Council of Shopping Centers. The discount of public REITs versus private transactions has blown out to the widest level in at least 15 years. Our ongoing monitoring of private transactions and deal flow continues to corroborate this thesis.

Despite these clear valuation disconnects, SKT, KIM, and KRG have essentially crashed in 2018 YTD so far, down 19%, 22% and 26% respectively at the time of this writing. There is now 35% upside for SKT to revert to what is merely a distressed valuation level of a 7.75% cap-rate, compared to its long-term median of 5.4%. KIM has 51% upside to our base case price target that implies a 6.75% cap rate, which is still way above what they've been selling their worst assets for. KRG has 63% upside to revert back to a 7.0% implied cap rate, which would still imply a much lower valuation for their entire portfolio than what they've been selling their worst, no-growth properties for in tertiary markets.

Update on PINC

During the quarter we increased our weighting in Premier, Inc. (PINC) on weakness following what we believe were unfounded worries over Amazon entering its main hospital Group Purchasing Organization (GPO) business and fears over large GPO clients not renewing contracts on similar economic terms, which has mostly already been disproven. A pricing comparison study of the 100 most frequently bought products by PINC's GPO members showed that competitor pricing averaged 72-121% higher than PINC's, and this includes Amazon Business. Additionally, the market remains worried over hospital utilization trends and the prospects for lower supply spend running through hospitals. While this is a legitimate fear, PINC has diversified their GPO business (~80% of total company EBITDA) and expanded their services to offer a variety of supply chain management services to non-hospital settings, including serving ambulatory surgical centers, urgent care clinics and smaller physician groups, as well as having many SaaS IT businesses and advisory/consulting services to help healthcare providers move towards a value-based reimbursement regime. Also, during the quarter the company gave commentary around the corporate tax reform, revealing that they would be a large beneficiary as their tax rate had been 40% and would now drop to 25%. Upon this disclosure, our forward EPS estimates immediately jumped by ~25% and we thought consensus estimates would have to soon follow with massive upward revisions, lowering PINC's

P/E multiple to 11.5x from 13x. This compares to the S&P 500's forward P/E of around 17.5x, despite PINC being an operationally and financially superior business compared to the average S&P 500 company. For context, the company IPO'd at a 20% forward P/E premium to the S&P 500 and now sits at a 25% discount. Its primary competitor MedAssets was bought out for 11x NTM EBITDA and 25x NTM earnings in 2016 in what struck us a somewhat distressed sale, as MedAssets had just lost one of its largest clients and had declining revenue growth. PINC now sits at 7.5x EBITDA and exceeded EBITDA expectations in their most recent quarter, while reaffirming good guidance. PINC has low cyclicality, high revenue visibility/recurring revenue (99% average GPO customer retention and 95% SaaS customer retention), solid organic growth, and operates within an oligopolistic industry.

While its shares are currently out of favor with investors, we believe now is the time to acquire more as the sentiment on PINC can turn 180 degrees at any point or it can slowly scale a wall of worry. The investment narrative could go from something at present along the lines of being "a low growth stock with a convoluted corporate structure and some cyclical headwinds that Amazon may want to compete with" to "PINC is a severely undervalued free cash flow compounder, a leader in a duopoly industry structure with 30%+ operating margins that is positioned for secular growth and is tackling one of the most important long term challenges in the United States--lowering costs for the healthcare system, that Amazon may look to acquire if it were truly interested in getting into hospital supply chain. It has excellent revenue visibility, extremely strong profitability, no net debt, and a structural advantage given that customers own the majority of the company (60%), are financially aligned, and can help vet potential acquisitions."

Update on PAR

A name we've highlighted many times publicly in the past is PAR Technology Corporation (PAR). In November the stock sold off dramatically from $11+ to ~$7.50 upon the news that two independent directors were resigning from the Board (out of a five-member board), creating a significant drag on the Fund's performance in November (though it was a large profit contributor for the year). Shares have yet to recover much. We continue to think PAR shares are materially undervalued due to ongoing corporate governance mishaps. Despite their ongoing actions, management's stated intention is to become a restaurant technology pure play and more software-centric. We believe prudent actions taken at the Board level to optimize corporate governance and sharpen management focus and execution on the large restaurant technology opportunity can potentially bolster PAR shares to multiples of their current price over the next few years.

Operational Update

We are excited that Kelli Walter joined us as COO during Q4. Kelli hit the ground running—no, sprinting like Usain Bolt and has really beefed up every aspect of our operations. One of the many projects Kelli has spearheaded so far has been relocating The Alpha Factory from Rice Village to the Greenway Plaza area. We invite you to come by and visit anytime so we can "share the Vosspel" with you.

The market is a wonder to behold and will progress through its inescapable repetition of bubbles and busts. Every new day reveals psycho-cultural afflictions, mass delusions and irreconcilable relative valuation mysteries worthy of a lifetime of investigation by psychologists and economists. While we will sometimes get frustrated from applying logic to an often-illogical game, our aim is to continue to focus on what we can control and stick to a disciplined application of proven value-investing principles. We are down on cost basis on over two-thirds of our long positions and almost one-half of our shorts. We think, therefore, that our existing portfolio has substantial embedded upside as it stands. Furthermore there should also prove to be plenty of additional opportunities to recycle capital into superb risk-reward situations, enabling the power of long term compounding to keep working in your favor.

Sources:

1: Real Capital Analytics, Inc.

<u>Disclosures and Notices:</u>

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The Russell 2000 index is an index measuring the performance approximately 2,000 small-cap companies in the Russell 3000 Index. The Russell 2000 serves as a benchmark for small-cap stocks in the United States.

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The Russell 2000 Value Index measures the performance of the small-cap value segment of the U.S. equity universe. It includes those Russell 2000 companies with lower price-to-book ratios and lower expected and historical growth values.

Using only liquid securities, the Credit Suisse Long/Short Liquid Index seeks to reflect the return of hedge funds as represented by the Long/Short Equity sector of the Credit Suisse Hedge Fund Index.

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