Long Cast ADVISERS LLC

Dear Friends:

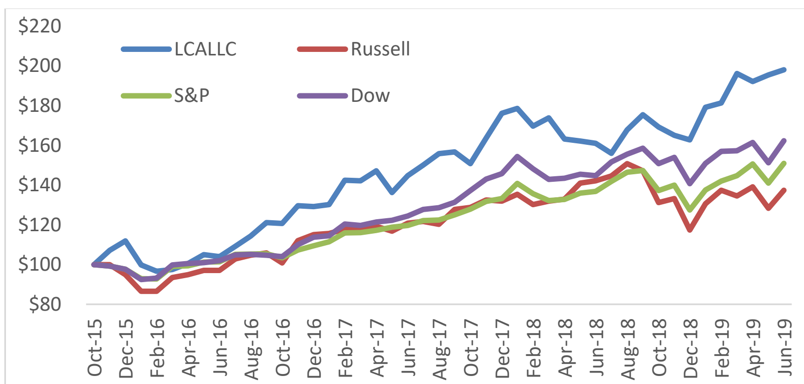
Cumulative returns on accounts managed by Long Cast Advisers increased 1% in 2Q19, net of applicable fees. This was worse than the baseline market indices. Returns for separate accounts managed by LCA ranged from -10% to +3% for the quarter.

YTD through quarter end 2Q19, accounts managed by LCA have returned 22%, better than baseline market indices. Since inception through quarter end 2Q19, LCA has returned a cumulative 98% net of fees, or 20% CAGR, ahead of the baseline market indices.

Because our portfolio is comprised of just a handful of typically small "off the beaten path" businesses that we tend to own for long periods, it is expected that returns will vary considerably from the baseline. As a reminder, LCA will not invest in companies exposed to the hydrocarbon or defense industries, a small effort to align capital growth, business ownership and personal ethics.

PERFORMANCE / PORTFOLIO HOLDINGS

	Long Cast	R2000	S&P	Dow
	Percentage Change			
2015 (2-mos)	12%	-5%	-2%	-2%
2016	16%	21%	12%	17%
2017	36%	15%	22%	28%
1Q18	-1%	0%	-1%	-2%
2Q18	-7%	8%	3%	1%
3Q18	9%	4%	8%	10%
4Q18	-7%	-20%	-14%	-11%
2018	-8%	-11%	-4%	-3%
1Q19	20%	15%	14%	12%
2Q19	1%	2%	4%	3%
YTD to 6/30/19	22%	17%	19%	15%
Cumulative chg	98%	37%	51%	62%
CAGR	20%	9%	12%	14%
LTM	23%	-3%	10%	12%



I'll write briefly below on the factors that impacted 2Q19 performance for the consolidated portfolio. Please keep in mind that since I don't use a model portfolio[1], individual account returns, holdings and weightings will vary. The differences between portfolio accounts is almost wholly based on the timing of when those accounts were opened. Contemporaneous portfolios are mostly similar and as account tenures grow their holdings and weightings should harmonize.

QRHC was the largest contributor to 2Q19 returns. It likely benefitted from the "halo effect" of a new Chairman Dan Friedberg who (among other things) bought stock at $2 / share, a then premium to the market price. Freidberg wrote an inaugural shareholder letter that is worth the time to read.

[1] The arbitrary buying / selling of stock based simply on the random timing of your decision to open an account seems absolutely absurd to me

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Going forward, sustainable appreciation in the company's intrinsic value will have to be driven by growth, cash flow and reinvestment at high rates. As demonstrated by the various letters I've written and published, I am frustrated by the lack of growth and the slow crawl towards profitability. Perhaps I'll be proven wrong but I am doubtful we have the right CEO or CFO for the job.

We own this company however, b/c the business has solid attributes and with the right nurturing can be very profitable. Hopefully, the new Chairman will see what I see, conduct his own interviews of exiting employees (there are quite a few, and I've done my own) and then fix the problems, which are all solvable.

I'll reiterate yet again that the biggest problem I see, and the one that if solved would most widen the opportunity pathway, is implementing a scalable technology platform. I've talked to executives in the waste brokerage industry and it doesn't take a lot of money to achieve this if you have the right people with the right intentions who know what they're doing. Alas, the inverse, makes scale impossible.

A logistics business is generally comprised of a robust technology platform + a sales team. Having one without the other is like going to the beach without a towel. Hopefully, with this new Chairman, there is at least a lifeguard on duty.

DAIO, **SIFY** and **INS** were leading detractors in 2Q19. The first two were negatively impacted (broadly speaking) by global trade / tariff concerns and more specifically, by peak auto cycle (DAIO) and "emerging markets off" (SIFY). INS, was the subject of a "bear raid" in the quarter. I wrote a bit about that on my blog. I'll briefly discuss more on this below.

DAIO (as a reminder) manufacturers capital equipment used to program microchips in small-volume runs. Auto is a big market for them and simple math drives that market opportunity: Chip / car and byte / car penetration is growing and this should expand the need for more chips programmed and therefore chip programming equipment.

It's fair to ask why we own a capital equipment manufacturer that supplies a cyclical industry at the peak of that cycle? The answer is that I like to own promising companies with strong management at a good price, and I think this is what DAIO represents.

On the face of it, 8x trailing EBITDA isn't such a "good" price, especially if EBITDA is cyclically declining. EBITDA however is understated by incremental R&D spending to support a novel and recently launched chip encryption platform called SentriX.

If that chip encryption platform *fails*, and management dials down to "normal R&D" (I assume 20% of revenues), this is trading at 5x trailing EBITDA, which doesn't seem unreasonable for a leading niche company with a solid management team that takes reasonable bets while conservatively managing its balance sheet.

If the platform *succeeds*, and we might not know for a few years, it would transform the company into something completely different, one with a potentially stable mid-teen ROE vs the current cyclical 0%-25% range. As a patient owner of sound businesses, this seems like one that could distinguish itself over time and is worth owning despite today's cyclical headwinds.

SIFY is an Indian telco and data communications company that's part asset lite services, part asset heavy infrastructure. The asset heavy side is mostly fixed telco assets and data centers, which it builds for itself and as a service for customers. They have six fully utilized data centers and four more under construction. It's growing and profitable and it is our small bet on future Indian Internet penetration. The business is a bit more capital intensive than we normally like, and maybe not as "moat protected" but management is doing many things right and if they could improve collections, that alone would fund substantial CAPEX. It trades by my calculation at ~7x EBITDA.

Two other holdings in the top-five, **CTEK** and **TBTC**, were not material contributors in the quarter but have recently announced news worth mentioning. CTEK hired a new CEO, Caleb Barlow, who until recently was a VP for IBM's IT Security division and founded it's "X-Force Incident Response" team.

I've seen models of success and models of failure when small companies hire large company folks as CEOs. Since it's impossible to know the future, we will have to wait and see. The current CEO Mac Macmillan made no secret of his desire to retire. Mac is expected to remain both on the Board and a large shareholder. I sent Caleb a note welcoming him to our company; it's appended here.

TBTC announced what amounts to a reseller agreement with a small Japanese IT company, Broadband Security, in the newly opened casino market in Japan. TBTC continues to expand its services to new geographies helping to support growth in installations, which feeds recurring revenues. I would like to see better cost scaling on the recurring revenue side. Management has the same goal and it's a solvable problem so would hope to see this change over time. In the meanwhile, you get a growing installed base with high returns on capital.

Getting back to INS, it presented some challenges and stresses in the quarter that made me reflect on the friction between the principles of a long-term investor rubbing up against a stock that moves far and fast.

We started acquiring INS ~$8. It went to $49. I generally like to make as few decisions as possible, but in that brief period one seemed thrust on me. Do I hold? Or sell? And if so, how much? Turning this over in my mind, I found a brilliant quote by John Neff: "When you feel like bragging about a stock, it's probably time to sell." That is a good and easy rubric to follow but on 2nd level thinking, nobody brags about selling a business below its intrinsic value.

Then the shorts came out and the stock was knocked down to ~$25. That ~50% decline in a top holding was demoralizing and called for some reflection. There are times to be a rock sturdy and unchanging, times to be a deeply rooted tree whose branches go with the breeze and times to be a tumbleweed voiced over by Sam Elliott. But under any circumstance, I am hard pressed to find a better industry than payment processing and a better business than one like this on the cusp of accelerating and sustainable growth. We used the sell off to buy more.

Finally, we've started acquiring shares in two new companies, both with good underlying businesses trading at low valuations and both with what I consider "hidden assets". If you look closely at your quarterly account statements you'll see them listed. If you want additional information please don't hesitate to ask.

CONCLUDING THOUGHTS: A PET PEEVE

One of my pet peeves in the investing world is when I ask someone how a company is doing and they tell me about the stock. It's as if, when asked "is that person a good baseball player" the response is based on the value of their baseball card.

There are a lot of analogies between investing and baseball, none more popular than Buffett's "waiting for the fat pitch." It makes me think of Ted Williams, career .344 batting average, with 521 home runs and a .482 on-base percentage. In 1941 he hit .406 and - as if you don't know - is famous as the last player to hit over .400. (Before Williams, Roger Hornsby did it *three times*.)

Imagine now, you go out and buy a book "Hit Like Ted Williams", and you read it and dog ear the pages and highlight the key parts. After you read the book, you go to a batting cage. How many pitches would you need to see to feel confident you could hit like him? How about against live pitching? How about in a game?

Obviously, there are differences between being a professional investor and a professional baseball player, and perhaps the biggest is the barrier to entry. Beyond just athleticism, there are various gating mechanisms in professional baseball that keep out non-professionals. But anyone can - and many anyones do - hang out an investment management shingle despite their lack of experience or expertise.

Which leads to another investing / hitting analogy. In both activities, you always risk looking like a fool and are always susceptible to being fooled. Only investing, however, encourages the skill of trying to sound smart while justifying whatever foolishness just occurred.

It takes time and experience and possibly innate skills (a lot of good investors are "on the spectrum") to understand the nuances of investing. Given my ~15 years as an investment analyst, I think I'm pretty good at interpreting financial statements. With only ~3 years as a portfolio manager, I realize I still have a way to go at predictably turning analysis and insight into actionable long-term decisions, but I think I'm on the right track. When ideas percolate up, my advisory board helps identify what I'm missing.

It remains my desire to grow LCA thoughtfully and incrementally. My goal is to spend my time investing in order to grow mine and my client's capital, not to build a large business with large business infrastructure.

Several new clients have joined since the beginning of the year and several existing clients have added new capital. If you know other like-minded and patient investors who would appreciate working with me, please let me know so we can arrange an introduction. 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 write.

Sincerely / Avi
July 2019
Brooklyn, NY

Welcome to Cynergistek! Inbox ×

avi fisher <avi@longcastadvisers.com> Tue, Jul 23, 1:18 PM (8 days ago)
to caleb, Mac, Paul

Hi Caleb. Since JD (inappropriately) cc'd you on an email he wrote, I thought I'd at least follow with a brief introduction and "welcome aboard".

I run an investment management firm focused on concentrated long term investing in small, well researched and well understood companies. We (for myself and clients) have been shareholders for two years and currently own about 180,000 shares of CTEK stock. This is a top-three position for the firm so I have a lot invested in your success, *more invested in fact than any non-employee director on your Board*. And unlike your Board, I continue to buy more.

I have a background as a sell side analyst at BMO Capital and CSFB covering mostly industrial services, including several years analyzing healthcare staffing and IT staffing, so I'm quite familiar with your end markets and business drivers. Based on this experience, I could confidently tell you that the entirety of our business is driven by growing volumes on the bill / pay spread of a man hour labor rate, but that ignores many other realities.

Rather, I think the real secret in business - your business, my business, and everyone's in between - is to delight your customers by solving their problems at a reasonable cost and margin. If you can do that while keeping employees engaged with interesting work and concurrently re-allocating capital wisely and efficiently, everything else in terms of stock price and valuation will take care of itself.

With this in mind, I hope you will please spend some time shaping your goals, mission and vision, for this year and the next five years, because in the absence of results (shareholders don't even know *last year's* results) we should at least understand your vision for the future. To help guide you, I highly recommend reading the shareholder letters by two CEO's - Jeff Bezos of Amazon and Mark Leonard of Constellation Software – to see what long term thinking really looks like in practice at a public company.

There is a lot of demand for the kinds of services Cynergistek offers and that ought weigh the scales favorably towards long-term growth, cash flow generation and reinvestment opportunities. I hope your efforts further improve the odds of success, and that you find the right path forward to nurture, grow and expand Cynergistek into a scalable and highly profitable business for many years to come.

Sincerely / Avi
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