January 2020

Dear Partners,

In the fourth quarter, 1 Main Capital Partners, L.P. (the "Fund") returned 12.4% net of fees and expenses[1], bringing YTD performance to 25.2%. Since its inception in February of 2018, The Fund has returned 10.7% net, compared to 19.0% for the S&P 500 and 8.5% for the Russell 2000 over the same period.

I hope to generate strong returns on our portfolio each year, as nearly all my net worth is invested alongside you in the Fund. However, it is important to repeat that the true success of our partnership will be determined by our performance over the long term, rather than in specific months or quarters. Given the valuation and outlook of our holdings, I remain optimistic about our prospects for winning together in the coming years.

Fourth Quarter Contributors[2]

Meaningful contributors to performance in the quarter included Alphabet Inc (GOOG), Altigen Communications (ATGN), Hemacare Corp (HEMA), KKR & Co (KKR), Mastech Digital (MHH), the Sanofi Contingent Value Right (GCVRZ) and Total Site Solutions Inc (TSSI).

Exited Positions

Hemacare Corp (HEMA), which was a meaningful contributor to performance in the third quarter, reached an agreement in the fourth quarter to be acquired by Charles Rivers Laboratories, a leading clinical research organization. I suspected that HEMA would make an attractive acquisition candidate when the Fund initiated its investment in the company. However, I was surprised by the timing and somewhat disappointed with the take-out price that management approved.

Mastech Digital (MHH) has more than doubled since reporting its third quarter results, which showed investors the trifecta they were looking for: strong organic revenue growth, margin expansion and significant free cash flow generation. Given the magnitude of multiple expansion, the Fund has sold its investment in MHH as the stock price reached a full valuation.

Sanofi Contingent Value Right (GCVRZ), which was profiled in the Fund's third quarter letter, appreciated significantly following an agreement between Sanofi and the Trustee of the contingent value right (CVR) to settle the outstanding breach-of-contract litigation for approximately 88 cents per right, well below $3-7 that I was expecting. While I thought that the CVR Trustee made a compelling case for a breach, a recent precedent case suggested that the burden to prove damages might end up with the Trustee. According to the Trustee, Sanofi may also have had plausible reasons for the delays in meeting its production milestone.

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[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 2019 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] Attribution is presented gross of management fees, expenses, and incentive allocations.

In order to minimize risk to CVR holders, the Trustee decided to accept a certain 88 cents instead of an uncertain $3-7.

Top 5 Positions

As of December 31st, the Fund's top 5 positions were Issuer Direct (ISDR), KKR & Co (KKR), MasterCraft Boat Holdings (MCFT), RCI Hospitality (RICK) and Total Site Solutions Inc (TSSI). Together, these accounted for approximately 45% of assets.

Issuer Direct (ISDR) is a communications and compliance firm focusing on the needs of its corporate issuer clients. The company's solutions include a news dissemination offering, which is marketed under the ACCESWIRE brand, in addition to a variety of other investor relations tools, such as webcasting, conferencing and disclosure software, that help clients with their SEC filings.

The company was built by its founder and CEO through a series of acquisitions which have increased its product offering and made it more relevant to clients.

Over the last few years, the company has been in the process of transitioning its business model away from project-based engagements to annual platform subscriptions, which has in turn increased the predictability of the business but has also temporarily suppressed revenue growth. Additionally, in the last year, the company was impacted by the rapid decline of its investor commentary business.

However, underlying demand for its core services has been very strong. ACCESSWIRE, which accounts for approximately 35% of total company revenues, organically grew by nearly 70% in Q3 and 40% YTD, excluding the decline in its commentary business. At a $6 million run-rate, this business still represents just a tiny fraction of its addressable market and is well positioned to grab share in the coming years.

ISDR's conferencing business, which organized 20 events of greater than $250k budgets in 2019, will likely organize 100-200 such events in 2020. Similar to its newswire business, the market opportunity for conferencing is large and the company is well positioned to capture share.

As we head into 2020, ISDR's revenue growth and margins should inflect while the company continues to look for opportunities to put its large cash balance to good use. With an undemanding valuation and strong balance sheet, I believe the odds of a good outcome are on our side.

RCI Hospitality (RICK) has been a drag on the Fund's performance since inception and remains our largest position as we head into 2020. In fact, the position is nearly 2x the size of the Fund's next largest holding. As we sit here today, RICK is late to file its annual 10-K with the SEC for the third time in as many years, had its auditor resign late last year and is under formal investigation by the SEC regarding a series of negative articles published about the company by an anonymous short seller. Ordinarily, these circumstances would cause me to realize a loss and move on. Instead, I have added to the Fund's investment in the company. As such believe it is appropriate for me to provide an update on the situation.

As a quick reminder, RICK is a holding company that owns three dozen gentlemen's clubs operating under various names and a rapidly growing 10-location sports bar & restaurant concept called Bombshells in some of the largest cities across the US. At under $20 per share, the stock is currently valued at approximately 5x FCF. The company has some debt which is easily supported by its strong cash generation as well as the company's ownership of a significant amount of its real estate and associated liquor licenses.

RICK's CEO owns 8% of the company and has shown himself to be a capable capital allocator. Importantly, there are ample opportunities for RICK to reinvest its FCF back into its business at very attractive returns, while at the same time reducing the company's share count through accretive share repurchases. Since 2015, RICK has made investments that have led to a doubling of operating cash flow, while also reducing its share count by over 15%.

However, the company's stock price has yet to follow its fundamentals due to the accounting troubles which are acting as an overhang. So, it is important to walk through a brief history of why RICK has been challenged in filing its annual report in a timely manner, why there is an SEC investigation into its practices and when these overhangs should be resolved.

It all began several years ago when several shareholders suggested the company upgrade its auditor to a larger, more nationally recognized firm. So, in 2017, RICK announced that it had appointed a top six national accounting firm as the company's auditor. At the time, the press release read: "With RCI's broadening national footprint, we decided it was time to make the change to BDO." Based on company filings as well as my conversations with management, there were no issues or disagreements with the old auditor.

In conjunction with changing auditors, RICK also initiated an effort to upgrade its financial reporting systems, including deploying a new ERP system. Delays associated with the new systems along with a more stringent audit process with BDO caused RICK to delay filing its 10-K twice in two years. After both delays, RICK eventually filed its 10-K with no restatements.

Then, in mid-2019, the SEC began an informal inquiry, which has since converted into a formal investigation, in connection with a series of negative articles published about the company by anonymous short sellers. While many of the accusations that the short sellers made were inaccurate, the gist of it was that the company was partaking in some related party transactions that it was not disclosing to shareholders and could potentially amount to theft.

In response to the SEC inquiry, the company's board formed a special committee that was tasked with conducting an independent internal review to investigate the matters raised by the short sellers. The special committee engaged an international law firm as an independent outside counsel.

The outside counsel, which was led by a former US Attorney with extensive experience in matters of this nature, began a comprehensive review that included (i) reviewing documents relating to the SEC inquiry and the anonymous internet articles; (ii) gathering and assessing relevant publicly available documents, including Secretary of State filings; (iii) reviewing and analyzing the Company's quarterly and annual filings with the SEC; (iv) running extensive searches on email servers and reviewing relevant documents; and (v) conducting appropriate interviews.

After a month's long process, during which management and employees of the company fully cooperated with the outside counsel, the special committee concluded that there was inadequate disclosure regarding several related party transactions and executive compensation, the amounts of which were insignificant to the company's overall profitability. For example, the company bought furniture for its restaurants from the brother of RICK's CEO. Also, the company's director of operations was the brother of a company board member and this connection along with his salary were not disclosed**.**

Clearly, these items should have been disclosed to investors. However, I doubt most shareholders would have a problem with any of the findings had they been disclosed appropriately to begin with. In fact, I believe that most public companies forced to undergo an extensive formal review would conclude with similar types of findings.

Importantly though, the additional disclosure had no impact on the company's earnings or cash flows since everything had already been appropriately expensed and accounted for in the company's financial statements.

However, in conjunction with the completion of the review in mid-2019, BDO resigned as the company's auditor. The audit firm wanted to take charge of the review, when instead they should have been comfortable that the former US attorney tasked with overseeing it would appropriately do his job. The company didn't see a need for multiple parties conducting similar reviews multiple times at a significant cost and understood that this would lead to them having to change auditors.

Notwithstanding its finding of internal control weakness and inadequate disclosure, BDO signed off on RICK's cash flow statements prior to resigning, including capex and buybacks – in my eyes, cash is king.

Since BDO's resignation, RICK has hired another national audit firm, Friedman LLP, and has been working with them to complete an audit of FY 2019 and to re-certify the prior audits. The company expects this to be completed by February, and that going forward it will file its financials with the SEC on a timely basis.

While the SEC review has yet to be resolved, I believe that the regulatory body will likely reprimand RICK for inadequate disclosure in its prior filings and reach some financial settlement with the company. I do not expect any fine to be material, since the goal of such actions is to protect shareholders of public companies, not to harm them.

The above issues have clearly caused RICK's shares to suffer, while the company continues to generate an abundance of cash that is being used to open new restaurants, buy additional clubs and buy back shares, the stock continued to bleed and is down nearly 50% from its 2018 high.

As we wait for the company's issues to be resolved, I appreciate that RICK's strong FCF is underpinned by a large portfolio of owned real estate, including a valuable property in NYC and other attractive locations in South Florida and Texas. I believe that this real estate is collectively worth significantly more than its book value of nearly $200 million, providing us with downside protection should the economy weaken at any point during our holding period.

To summarize, based on the company's valuable assets, capable management team and strong cash flow, I have a tough time seeing how we lose much and can easily see us making multiples of our capital in this investment in the coming years.

Total Site Solutions Inc (TSSI) is a systems integrator and service provider to the modular data center market. The company helps its large enterprise clients build and maintain a variety of hardware and software used in their modular data centers across the country.

The company originally went public in 2007 through a special purpose acquisition corporation (SPAC). At the time, the company designed and built data centers, mostly for the government, and looked a lot like a project management business. Its revenues were lumpy, fixed costs were high, margins were low, competition was increasing, and the company made a series of acquisitions to defend its market position and smooth out revenue. Over this period, the company didn't generate profits and the stock declined by nearly 90%.

In 2011, a new CEO was brought on and set out to re-focus the company on less-competitive, higher margin opportunities. Under his leadership, in 2013 the company acquired its modular data center systems integration and maintenance business. Over the next several years, TSSI sold non-core assets to strengthen its balance sheet, while eliminating a significant amount of its overhead.

Today, the company is focused entirely on the modular data center market. Modular data centers allow its users to scale their capacity over time on an as-needed basis, compared to traditional data centers which require much more capital investment for greater upfront capacity than is needed today. This allows for a steadier pipeline of service work for clients, who require ongoing planning, configuration, rack construction, server integration, deployment and maintenance.

According to industry reports, the modular data center market is expected to grow at a double-digit CAGR in the coming years. As the primary vendor working with Dell's server clients, TSSI stands to directly benefit as Dell's clients expand their data center capacity.

Until recently, the company has been providing its value-added services for its clients on consigned materials which it hasn't taken title of. However, on its 2019 second quarter call, TSSI announced that it had begun to pursue opportunities to become a value-added reseller (VAR) for some of its data center clients. In these cases, the company will procure and then resell the hardware and software that are integral to its services, effectively taking market share from traditional VARs by cutting them out and earning a small margin for its work.

The revenue opportunity associated with this initiative is very large for TSSI. For context, the company generated annual revenues of approximately $20 million, while it handles over $1 billion of hardware for its clients per year. Importantly, due to the nature of the deals, TSSI will not need to make any meaningful working capital investments to win this business.

During its third quarter call, TSSI reported on its progress under the VAR opportunity. On it, management said that they expect fourth quarter revenue to be higher than the first three quarters combined. Additionally, the company said that it expects fourth quarter EBITDA to nearly double the first three quarters combined.

In follow-up conversations with management, I learned that Q4 is not expected to be a one-hit wonder and that the company's pipeline of VAR opportunities heading into 2020 is very promising. Should it win several of these opportunities, revenue and earnings should scale exponentially in the coming years.

Despite its share price doubling over a very short period since the Fund's involvement, TSSI's absolute valuation remains undemanding. As such, I have allowed the position grow in size and am hopeful that the company can execute on a large pipeline in the coming year.

Other top 5 positions: there have been no material changes to the investment theses of **KKR** and **MCFT** since they were profiled in previous letters.

Paid to Grow

In past letters, I have outlined why I prefer investing in businesses that can compound their value at attractive rates for long periods of time over ones that should be shortly re-valued by the market and sold for a quick gain.

Some reasons for this included that they tend to be: i) higher quality businesses with less business-specific risk, ii) ones that I am more familiar with since I have followed them for longer, iii) more tax efficient for their owners since they can reinvest their profits without exposing their holders to the double taxation that comes with realizing capital gains or dividends.

When I look at long-term compounders, I tend to categorize them into three buckets:

1. *Cap-lite growth Co's* – these are businesses that require very little capital for growth but are growing their revenue, and thus enterprise value, at an attractive rate. Since there is no need to reinvest much back into the business to grow, they can distribute most of their earnings to investors via buybacks or dividends, while the appreciation in business value (driven by earnings growth) flows to equity holders as well. A good example of this is Alphabet Inc (GOOG); build it once, sell it billions of times, return your profits to shareholders while you keep selling more.

2. *Cap-intensive growth Co's* – these are businesses that require capital to grow, but the returns on the reinvested capital are attractive. While these companies don't distribute much cash to shareholders since most of it is reinvested, they grow earnings at an attractive rate because of the strong ROICs. A good example of this is a rapidly growing differentiated retail concept; prove the model, then build as many times as you can.

3. *Negative capital growth Co's* – these are businesses that not only grow with very little capital investment but are capitalized in such a way that they distribute *more* than they earn in profits as they grow. A good example of this is a levered franchisor such Domino's Pizza Inc (DPZ).

Each of these three buckets have individual nuances that an investor should consider when evaluating a growth company. There are also companies that shift from one bucket to the next as their business matures or evolves.

However, negative capital growth cos are unique because, unlike cap-lite growth cos or cap-intensive growth cos, they can actually sustainably pay investors *more* than they earn in profits as they grow, and as such can end up selling for much higher effective FCF yields than their headline multiples may suggest.

A great example of a business that pays its shareholders twice when it grows is Domino's Pizza (DPZ), which is a position initiated by the Fund during the third quarter. DPZ is the highly recognized and largest pizza company in the world, selling more than 3 million pizzas each day throughout its global system. Nearly all of DPZ's stores are owned and operated by franchisees who pay the company royalties in exchange for using its brand and receiving support in the management and operations of their locations.

At 26x consensus 2020 earnings, DPZ doesn't screen as a particularly cheap stock; one might even say that its growth is already priced in. However, for a negative capital growth co, I think one should look at the sum of the earnings yield + the cash flow available from re-levering the business each year. On this basis, company looks much cheaper. Let's discuss.

The company's franchisees have been driven to open more locations each year due to the strong unit economics that they have enjoyed, with less than 3-year cash-on-cash paybacks on new stores. This can be seen when looking at DPZ's location count, which currently stands at over 16k units, up from less than 10k units in 2011.

Over the next 5 years, DPZ expects its location count to grow to over 25k global units. Amazingly, pretty much all the capital needed for this unit growth will come from the company's franchisees, leaving very little reinvestment need for DPZ. At this 7% expected unit growth CAGR, the company would likely grow revenue and EBTIDA at mid-single digits and high-single digits, respectively.

Even with this attractive growth profile, DPZ will have to reinvest almost none of its earnings back into the business given that the new units are being funded by franchisees. As such, at 26x earnings and 100% payout ratio, the earnings cash yield would equate to approximately 3.8%.

Additionally, DPZ will likely maintain its leverage ratio of approximately 5x as its EBITDA grows. This level of leverage is appropriate for a company that takes a royalty on system-wide sales, which are diversified across operators and geographies. Assuming a high single digit annual EBITDA growth rate, the new leverage taken on in to maintain a constant leverage ratio as EBITDA grows equates to an additional debt cash yield of approximately 2.5% that can be returned to shareholders each year.

Between the earnings, and added leverage, the distributable cash yield looks more like 6% than 3.7% and makes DPZ look more like a company valued at 16x distributable FCF than 26x.

Of course, in addition to the 6% cash yield that could be distributed to shareholders annually, the company should still grow its earnings, and equity value at approximately the same rate as EBITDA.

In summary, negative capital growth cos, such as growing franchisors with minimal operating leverage and strong debt capacity are sometimes overlooked by market participants because of their high headline multiple. However, if their growth is durable, they typically end up generating nearly as much cash through balance sheet expansion, as they do from their operations, which means their effective cash yields are higher than the earnings yield implies. I believe we have found such a winner in DPZ.

<u>Outlook</u>

In previous letters, I have suggested that US money managers have appeared overly bearish given the strong consumer, who has been benefiting from solid wage growth and low interest rates. Recently, it seems as though the pendulum has swung in the other direction, with expectations for a recession lessening and investors believing that the bull market may very well continue.

The much-improved sentiment has likely been driven by easing monetary conditions, a de-escalation of the US/China trade war and the calculation by investors that President Trump is unlikely to do anything that rocks the boat too much in an election year.

While I have not changed my views on the economic outlook much over the last two years, I acknowledge that holding the consensus view is as uncomfortable as holding an out of consensus one since neither I nor anybody else knows exactly when the tides of the economy or market will turn. It is for this uncertainty that investors in equities are compensated with excess returns for owning stocks over cash or bonds.

Absolute market valuations are above average, but still not extreme. The S&P 500 sells for a 19x 2020 earnings estimates, which corresponds to an earnings yield of approximately 5% (and growing), and still appears cheap when compared to the 10-year risk free rate of less than 2% (while not growing).

The economic outlook around the world seems constructive for now. With this backdrop, we will continue to focus on owning high quality businesses at attractive valuations that should do well over our long-term investment period.

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

Monthly Performance Summary[3]

2019	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
1 Main Capital Partners - Gross	4.6%	7.5%	-1.9%	2.2%	-6.9%	1.4%	4.1%	-1.2%	2.8%	4.0%	7.1%	2.9%	29.2%
1 Main Capital Partners - Net	4.5%	7.4%	-2.0%	2.1%	-7.0%	1.2%	4.0%	-1.3%	2.7%	3.8%	5.8%	2.2%	25.2%
S&P 500 index - incl dividends	8.0%	3.2%	1.9%	4.0%	-6.4%	7.0%	1.4%	-1.6%	1.9%	2.2%	3.6%	3.0%	31.5%
Russell 2000 - incl dividends	11.2%	5.2%	-2.1%	3.4%	-7.8%	7.1%	0.6%	-4.9%	2.1%	2.6%	4.1%	2.9%	25.5%

[3] Performance Data is presented for the Fund's Class A Interests, and are 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 2019 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.

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