

Portfolio Commentary

This article by Michael Melby is excerpted from a letter of [Gate City Capital Management](#).

The Fund generated an attractive absolute return for investors in the third quarter while underperforming the small- and large-cap indices.

TheStreet (TST), Dawson Geophysical (DWSN), and Canterbury Park (CPHC) were the Fund's top performers. TheStreet (TST) reported strong Q2 2017 results that were well-received by the market. Dawson Geophysical advanced as sentiment surrounding the energy services sector improved. Canterbury Park moved higher as the company continued to progress on plans to repurpose a portion of the company's excess land holdings. PICO Holdings (PICO) and Scott's Liquid Gold (SLGD) detracted from performance during the quarter. Of note, after quarter-end PICO Holdings announced that the company was reviewing strategic alternatives including a potential sale of the company.

The Fund ended the quarter with 18 companies in the portfolio. The largest position was 15% of the portfolio and the top five positions represented 50% of the portfolio. The Fund added three new companies during the quarter and effectively exited our position in Precision Auto Care (PACI) after the company was acquired by an affiliate of Icahn Enterprises. By sector, 24% of the Fund is in real estate (primarily land), 16% of the portfolio is invested in water assets, 16% in energy, 8% in consumer products, 6% in media, 5% in industrials, 5% in gaming, 3% in defense, and 18% in cash.

The average portfolio company has a Price/Book ratio of 1.1x and trades at 7.5x trailing EBITDA. These valuation metrics compare favorably to the S&P 500 which has a Price/Book ratio of over 3.0x and an Enterprise Value/EBITDA ratio of over 13.0x. The portfolio has a weighted-average market capitalization of \$135 million and an average enterprise value of \$110 million. As of quarter-end, all but one of our portfolio companies had more cash than debt on the balance sheet.

In our Q2 letter, we highlighted how we had recently spent more time researching companies in the energy sector. Even in a market where we consider many companies to be overvalued, we found several companies in the energy sector that had many of the qualities we look for including large cash balances, owned assets, and the potential to generate strong free cash flow. In this letter, we provide our investment thesis on Macro Enterprises Inc. ("Macro Enterprises", "MCR", or the "Company"), a Canadian pipeline construction company that we expect to benefit from increased infrastructure spending in Alberta and British Columbia.