OTSI KETA QUARTERLY

Twenty-Ninth Edition - July 2017

Q2 2017

Otsi Keta Quarterly is designed to share insight on both current performance and future potential.

IN THIS ISSUE...

QUESTIONS...

Contact us at:

312.473.3982

F. William Schwarz, III
bill@otsiketacapital.com

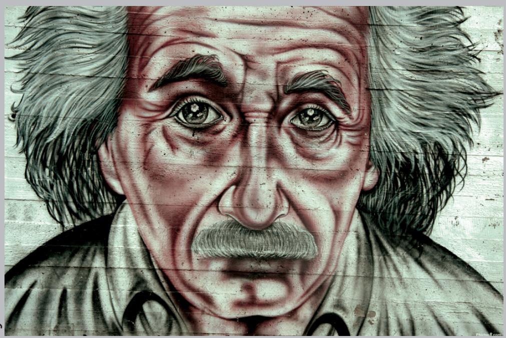
Frederick P. Rollins, Jr.
fred@otsiketacapital.com

We were reminded recently of an article we wrote on compounding capital in 2010. The occasion that brought this piece to mind was what has been affectionately called Bobby Bonilla Day, or for baseball's New York Mets, July 1st. July 1st is the day the Mets pay Mr. Bonilla $1.19MM. They have been paying him this amount every year since 2011 on July 1st. The Mets recent payment was their seventh, and they only have 18 more payments to go.

At a time when we hear more about sports heroes going broke than retiring comfortably, the Bobby Bonilla story is a nice change. In 1999, as an aging player in the Mets organization, Mr. Bonilla approached the Mets with a proposal to defer payment on his last contract year of $5.6MM for 25 annual payments of $1.19MM starting in 2011. The Mets' owners, the Wilpon family, believed that given the previous two decades of amazing investment return, that it was a smart play to make the deal. The Bonilla deal equates to an 8% compound return over the 35-year agreement. The Wilpon logic was that they could compound at greater than 8% annually and would come out ahead. In 1999, at the height of the Internet bubble, Mr. Bonilla went against the crowd. Time will tell who got the better deal, but it is looking pretty good for Mr. Bonilla at the moment. His current annual payment is twice the $535,000 league minimum in 2017 for active players.

Below is the article from 2010 that compared historically great investments to a steady 8% compound growth.

Power of Compounding



by Photos8.com

The rumor is that when Albert Einstein was asked to name the greatest innovation in human history, he simply replied "compound interest." We are not so sure about the authenticity of the quote, but the math is certainly compelling.

Our desire to compound our investing partners' capital is why we favor management teams that profitably deploy their cash within their businesses, or through shareholder-friendly actions like share buybacks, debt reduction and dividends. In essence, keep what you can compound at a high rate within the businesses, hold some cash for future endeavors and distribute the rest. It is important to remember that cash, over long periods of time, has a negative expected value due to inflation.

To drive home the importance of compounding, we have borrowed a concept from annual reports that Warren Buffet wrote to his investors in the early 1960s. The examples on the following page, like Buffet's, are meant to drive home the financial advantages of good assets, solid rates of return and long time horizons.

Continued on page 2...

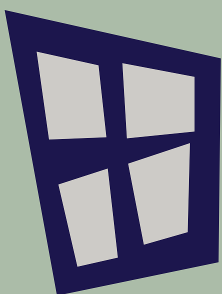
Continued from page 1

Here are two historical investments compared to the value created by a consistent 8% compound rate over the same period.

Investor	Investment	Cost	2010 Estimated Value	Joys of Compounding at 8.0%
William H. Seaward for the Federal Government of the USA	Alaska Territory from Russia in 1867 for 2.3 cents per acre	$7,200,000	$161 Billion*	$433 Billion
Peter Minuit	Manhattan Island in 1626	$24	$214 Billion**	$763 Billion

*The Alaska 2010 estimate based on $514 per acre, which is also consistent with current federal taxes paid by the state discounted by the current rate on 10-year Treasury.

**Manhattan Island 2010 estimate based on $345 average price per buildable square foot – source Christopher Begg East Coast Asset Management.



The Window Indicator

The shipping season is in full swing on the Great Lakes this year. Many of the familiar freighters are regularly traveling the lakes hauling cargoes of iron ore, coal, agricultural commodities and limestone. The Great Lakes continues to be a necessary conduit for the steel, power and construction industries in the Midwestern United States. But did you realize the "green" nature of a watercraft that is made of all steel with a stack or multiple stacks that belch exhaust? The following article comes from the Lake Carriers Association:

Waterborne commerce is the greenest form of transportation. It's simple physics. Because there's less friction when moving through water, less power is required. As a result, Great Lakes freighters use less fuel and produce fewer emissions in moving a ton of cargo than trains and trucks.

A 2013 report by the U.S. Army Corps of Engineers confirms maritime's greenness. The Corps determined that a Great Lakes freighter sails 607 miles on one gallon of fuel per ton of cargo carried. A locomotive travels just 202 miles on a gallon-per-ton basis and a truck a mere 59 miles using the same measure.

Marine is also superior in terms of carbon dioxide emissions. A cargo of 1,000 tons transported by a laker produces 90% less CO2 than the same amount moved by truck and 70% less than a thousand-ton load moved by a train.

The environmental benefit of those facts becomes even more apparent when they are upscaled to actual moves. For example, it would take seven unit trains, each with 100 cars, to equal one cargo carried by a 1,000-foot-long laker. Transfer that cargo to trucks, and 2,800 would be needed to deliver what one ship does each trip. Now the fuel savings and reductions in emissions have skyrocketed.

The Lakes fresh water environment makes possible another green side to Great Lakes shipping. Corrosion is slight on the Lakes, so a well-maintained hull can last indefinitely. As a result, ships are constantly modernized, thus saving the environment the raw materials that would be consumed by new construction (not to mention saving customers the costs related to new builds).

The steamship CASON J. CALLAWAY is a perfect example of the longevity and reinvestment made possible by the Lakes freshwater environment. When launched in 1952, the ship was 629 feet long and had a rated capacity of 22,064 tons per trip. In 1974, the vessel was lengthened by 120 feet, which increased its carrying capacity to 28,336 tons per trip. Then in 1982, the vessel was converted to a self-unloader, which allowed it to carry more cargos each season. In the deep sea trades, these increases in efficiency would have required at least one, if not two new builds. New engines are another way lakers reduce their carbon footprint. The past few winters have seen several vessels outfitted with new powerplants that use even less fuel and further minimize emissions.

Other steps to enhance the industry's environmental performance include use of environmentally acceptable lubricants and water-lubricated bearings.

Perhaps nothing better illustrates Lake Carriers' Association's (LCA's) commitment to the environment than the effort to find a solution to the worldwide problem of ballast water transport of non-indigenous species. Even though lakers never leave the system and so have never introduced a non-indigenous species, LCA has been a pioneer in developing Best Management Practices (BMPs) to minimize the potential that lakers' ballasts might spread an exotic introduced by an oceangoing vessel. As far back as 1993, LCA implemented a plan to address the ruffe in western Lake Superior, the first ballast water management effort in North America. The U.S. Fish & Wildlife Service declared the plan the "cutting edge of technology."

Then came groundbreaking research on filtration of ballast water. More BMPs followed, and then a plan specific to viral hemorrhagic septicemia.

Today, LCA members have undertaken initiatives of their own to further advance knowledge of effective means to address introduction and spread of aquatic nuisance species via the ballast water on oceangoing vessels.

Next time you look out the window near the Great Lakes waterways and see a boat that is large enough to cast a shadow over your home, think green. Until next quarter, enjoy the scenery outside your window. I know we will.

OUR PORTFOLIO

Investors seem pretty spooked about the world today. However, the companies in our portfolio are increasing the capital allocated to grow their businesses.

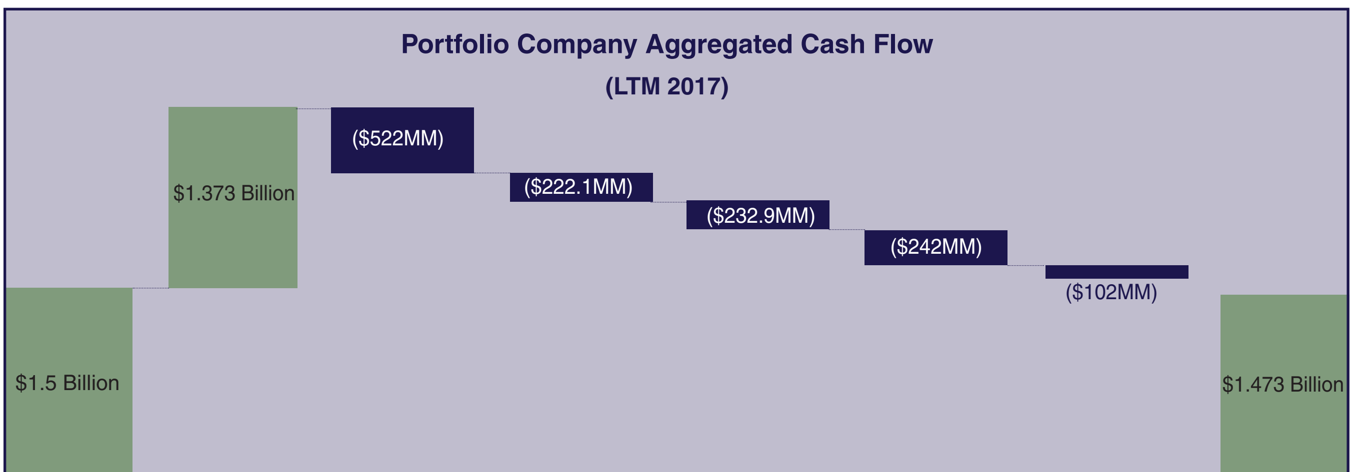
The OKFF portfolio ended the quarter with 18 holdings. As investment managers, we continue to buck the trend of thinking about portfolio construction as the only opportunity to outperform the averages. Don't get us wrong, we recognize the benefits of diversification and risk management. We even think some of the research on smart beta is compelling for investors. We just believe that increasing our depth of knowledge about the companies we are investing in is time well spent and that harmonically tuning our portfolio for all possible market swings is more the tail wagging the dog.

While the bulk of our time and efforts are spent on bottoms-up analysis of specific companies, we also from time to time like to look at our holdings aggregated together. It is no secret that we keep a close eye on cash flow and capital allocation within our investments. Cash flow and cash flow trends tell us a lot about the state of the business today. And, capital allocation is our best indicator of a company's priorities. If you want to know what someone values, look at their budgets. While the companies in the portfolio change over time, the aggregate portfolio analysis gives us a glimpse at how managers in our space are prioritizing the use of capital.

When we compare how our portfolio companies are allocating capital today versus coming out of the great recession in 2010, a couple of things stand out:

- The biggest change is the amount of operating cash flow (OPCF) that is being reinvested in the business through capital expenditures. Our portfolio of companies in 2010 spent 22% of their OPCF on capital expenditures; today they are reinvesting 38% of their cash flow.
- The bulk of the increased spending is coming from a reduction in special dividends and to a lesser extent common dividends. Total dividend spending as a percentage of OPCF has dropped from 25% to 17%.

Companies in our portfolio have almost doubled the percentage of OPCF they are dedicating to debt reduction. We believe these shifts in spending priorities are largely positive and represent a significant behavior change within the small cap value universe where we operate.



	Beginning Cash +	Operating Cash Flow -	Capital Expenditures -	Acquisitions/ Investments -	Dividends -	Share Repurchase -	Debt Reduction =	Ending Cash
2017 % of OPCF		100%	38%	21%	17%	18%	9%	103%
2010 % of OPCF		100%	22%	15%	25%	16%	4%	82%

Maybe the biggest indicator that management teams are finding investment opportunities: In 2010, our portfolio companies were reinvesting on 82% of their operating cash flow, and today that same calculation indicates they are reinvesting 103%.

OUR PERFORMANCE

For the second quarter ended June 30, 2017, the Otsi Keta Focus Fund was up 4.30%. Year to date, the Fund was up 4.83%. Since inception, the Fund has returned 128.75%. All Otsi Keta Focus Fund numbers mentioned are net of all fees and expenses. Please see the table below to review the performance of Otsi Keta Focus Fund Limited Partnership versus competitive indexes.

Fund Name	ROR 2nd Quarter 2017	ROR YTD June 30, 2017	ROR From Inception (May 7, 2010)
Otsi Keta Focus Fund Limited Partnership*	**4.30%**	**4.83%**	**128.75%**
Russell 2000 Index (^RUT)	2.18%	4.35%	110.67%
Russell 2000 Value (^RUJ)	0.67%	0.54%	87.40%

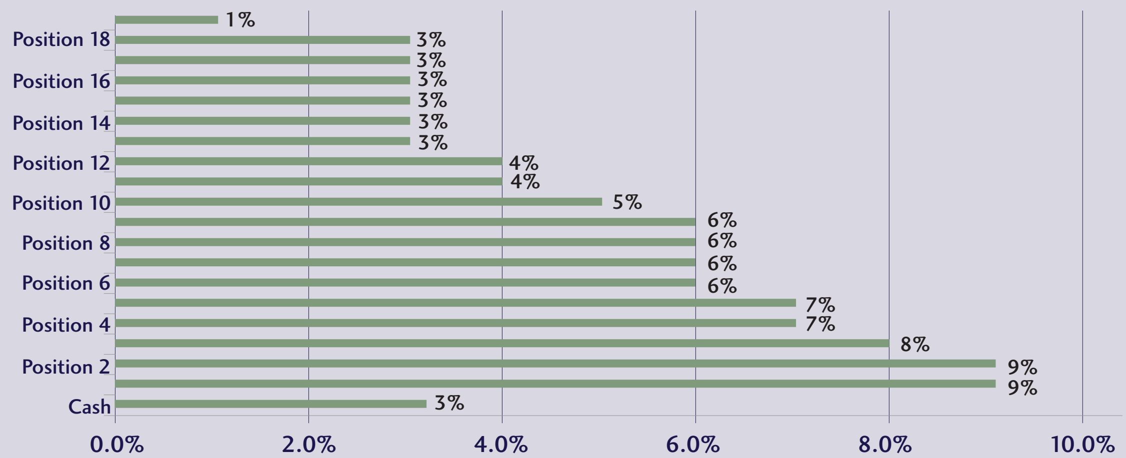
Sources: Otsi Keta Capital and Russell Investment
*Note: All OKFF performance data is shown net of all fees and expenses and is based on an investment with the maximum charge of 1.5%/10%.

The second quarter of 2017 saw smaller companies improve, though they still lagged the tech-laden NASDAQ 100 and the S&P 500. Small company indexes should see improvements as the year moves on and the domestic economy continues to improve. The portfolio experienced some change in the second quarter. Specifically, we increased our position in a couple of holdings, added a new one and sold:

- A smaller holding, Malibu Boats (MBUU), when it reached fair value.
- A longer term holding, Terra Nitrogen (TNH), as the nearer term prospects for fertilizer looked questionable due to a robust global crop and squeezed margins at the farm.
- Syntel, Inc. (SYNT), the Troy, MI-based call center business, did not meet our criteria for remaining in the portfolio after extensive conversations with management.

As the summer is upon us, activity slows down on Wall Street. We will look to capitalize on any situations that get amplified due to lighter volumes. Enjoy the summer!

Otsi Keta Focus Fund's Position Size
(Quarter ending June 30, 2017)



F. William Schwarz, III
Partner
direct: 810.247.3133
bill@otsiketacapital.com

Otsi Keta Capital, LLC
110 South Third Street
Suite 206
Saint Clair, MI 48079

312.473.3982

Frederick P. Rollins, Jr.
Partner
direct: 810.357.8566
fred@otsiketacapital.com

OTSI KETA CAPITAL