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Artko Capital LP

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Dear Partner,

For the second calendar quarter of 2020, an average partnership interest in Artko Capital LP was down 11.4% net of fees. At the same time, investments in the most comparable market indexes—Russell 2000, Russell Microcap, and the S&P 500—were up 25.4%, 30.5%, and 20.5% respectively. Our detailed results, related footnotes and subsequent events are available at the end of this letter. Our results this quarter came from mild portfolio declines in Recro Pharma, Gaia and Research Solutions while our Shyft Group holding (formerly Spartan Motors) contributed to improving the overall performance.

	3Q19	4Q19	1Q20	2Q20	YTD	1 year	3 year	Inception 7/1/2015	Inception Annualized
Artko LP Net	7.9%	17.4%	-37.4%	-11.4%	-44.5%	-29.1%	-8.2%	12.0%	2.3%
Russell 2000 Index	-2.4%	9.9%	-30.6%	25.4%	-13.0%	-6.3%	2.0%	23.4%	4.3%
Russell MicroCap Index	-5.5%	13.5%	-32.0%	30.5%	-11.2%	-4.8%	0.9%	15.1%	2.9%
S&P 500 Index	1.7%	9.1%	-19.6%	20.5%	-3.1%	7.5%	10.7%	66.5%	10.7%

On Operating Leverage and How We Win

“The farther backward you can look, the farther forward you can see” – Winston Churchill

The second quarter of 2020 continued to see a slow sell off in some of our biggest holdings, most of which have reported solid results and guidance; while the most speculative holdings within the small and large capitalization indexes continued to surge, buoyed by a firehose of equity inflows via very generous fiscal and monetary policies and a euphoric gambling attitude by the marginal market participant. That this has been an unpleasant turn of events is an understatement and has led to significant soul searching on whether a concentrated, contrarian oriented, micro and nanocap strategy can recover and continue to work in the long term. The short answer is we certainly believe there is room for our strategy to recover and continue to work in the long run, albeit with a bit more difficulty given the stock versus company market mentality problem, while refining and making marginal changes to the overall process. So what problem are we talking about here? It is the problem of the definition of “the stock market.” At the heart of it, the stock market is a market where participants exchange fractional ownership of 1000s of companies which are called stocks. While this may seem like an obvious statement, it is not called “fractional ownership of companies market” and for a lot of market participants the term “stock” becomes something of a cognitive dissonance from what it truly represents and takes on a meaning of its own. To put another way, the market has participants that are interested in investing in companies underlying the stocks and for them the stock market is a medium through which they can invest in those companies. The market also has a speculative arm of those that invest in stocks and for whom the underlying company economics matter less, if not at all and the trading behavior of the instruments matter more. These parties are more interested in the patterns of the stock prices and pay close attention to actions of buyers and sellers. In general, they tend to be more short term oriented and provide liquidity for the former. A healthy, functioning stock market will have a good mix of both with occasional bouts of speculation in various pockets, but with the price discovery or a value weighting mechanism still intact. What we are witnessing today is almost a complete domination of the speculative arm of the market, impervious to the deep recession we have found ourselves in, chasing momentum in stocks. With the United States Federal Reserve, the Fed, through a number of policies and statements, essentially signaling to the market

that they consider a declining market “bad” and will unleash significant firepower to prevent substantial capital market declines, the hereto implicit “Fed put” has now become explicit. This has clearly removed any sense of rationality from the marginal market participant and the market has truly become an exchange of “stocks” versus an exchange of “ownership of companies” more resembling a scene of a Black Friday morning at Best Buy rather than a typical orderly Wednesday afternoon at a grocery store.

Unluckily for us, but more fortunately in the long term, our strategy involves buying the companies that neither have the ability to participate in the government created equity flow firehose, due to our focus in buying the stocks of the companies that are too small to participate in passive or active market trends, and too illiquid to attract any volume creating momentum strategies. While this is obviously by design, it certainly does not feel good to watch the market pass you by as day traders clamor for shares of bankrupt car rental agencies and fraudulent payment and electric car companies and ignore the opportunities in the nano and microcap space. So, the real question remains, will the market revert to a healthier, more rational functioning medium for exchange of ownership of companies based on their underlying values or continue to remain a gamblers paradise for the foreseeable future? If history has taught us anything, is that over the long-term human nature is predictable, and after bouts of euphoria and irrationality a period of normality does return.

Of course, you cannot be an investor in the stock market and cry sour grapes when it does not work the way you want it to. While we certainly fashion ourselves as a “private equity in public markets” partnership, and we have had success in having a substantial number of our past holdings involved in value creating transactions, at the end of the day we are invested in publicly traded stocks and have to invest with a strategy that will make the marginal market participant want to pay more for that stock than our original cost. So, what makes stocks go up? Pretty simply put: growth in revenues and cash flows/earnings. Companies that can show consistent growth in both are much more likely to be rewarded with higher multiples and get credit for implied future growth than those that do not or whose growth is masked by short term events, and will be placed in a “market time out” until the growth resumes. That is essentially what has happened to our portfolio this year: the market sold off our companies back to their net asset/balance sheet values and it is taking, a semi skeptical, wait and see attitude. What has exacerbated this situation is our bet on the operating leverage of our companies, which is the heart of our strategy. While “old school” value investing involves buying companies at cheap price to book values and hope they revert to the mean, our strategy involves buying companies at balance sheet prices and with the expectation that their fundamental results missed by the market will make them valued as growth companies in the long term. The market has consistently underestimated the operating leverage of companies on the way up and on the way down, which is where we generally like to find most of our ideas, a lesson we learned early on in our career from Michael Moubisan (formerly of Legg Mason) and have reliably witnessed work a substantial number of times over the last two decades. In other words, due to companies investments in their fixed cost base, the growth in earnings and cash flows tends to be in multiples of its revenue growth as most of the revenue growth will tend to fall to the bottom line as a high marginal contribution. The vast majority of our portfolio, which we will take you through in the rest of the letter, has an expectation of intermediate high cash flow and earnings growth off a growing revenue base that in a return to a healthier, more rational market should result in company and of course, underlying stock values, at price levels substantially higher than experienced prior to this calendar year. We have sold a number of our holdings over the first half of the year for positive and negative reasons and added a few new names that we believe will provide a substantially better return opportunity in an economic recovery; however, changing a portfolio with our liquidity profile more resembles the movements of an ocean carrier than a swift sailboat and expect more marginal changes and additions in

the coming year as we look to capitalize on the aforementioned factors and nano and microcap valuation recoveries.

Core Portfolio Sales

- Viad (VVI) – In the first half of 2020, in what is likely the biggest disappointment of our partnership’s five year history, we sold our entire holding in Viad, which declined over 70% from its 2019 year end, at prices between \$17 and \$20, as the company’s two core businesses, global event and conference management and hotels and attractions faced, what we consider, an insurmountable road back in a post-Covid world. As we have written previously we are allergic to debt and most of the time have an expectation of a value unlocking event for an investment to qualify for inclusion in our Core Portfolio. Viad was well on its way to spinning off or selling its hereto valuable Pursuit, hotel and public attractions, business; while marginally adding to its debt levels via accretive tuck in acquisitions. However, the Coronavirus and economic events of 2020 left both of their business segments, which rely on close human interaction, in tatters, likely to earn very little revenue this year and setting its earning power back a half a decade. In the meantime, the company continues to burn \$10s of millions of cash, adding to their sudden dangerously high debt levels, requiring continuous covenant waivers from their lenders. A combination of leverage, a semi-permanent decline in earning power and the likely disappearance of a near term value unlocking event made holding our investment in Viad, as a Core Portfolio holding, an untenable proposition. We will keep a close eye on this company and we will be cheering for the company’s recovery from the sidelines and may potentially take a flier as a small position for our Enhanced Portfolio down the line.
- Sharps Compliance (SMED) – 2020 was not all bad news for our holdings and we have had a chance to participate in some wild speculation of today’s markets via our position in Sharps Compliance which at one point surged almost a 100% from its year end closing price of \$4.22 on the hopes that the medical waste disposal company will have an opportunity to participate in the significantly higher medical waste volumes as a result of Covid related activity. Sharps was a perfect example of our Core Portfolio strategy where we patiently added to the 10% position at what we considered “balance sheet” prices, i.e. the value of its working capital and incinerator was close to our mid \$3s purchase price. In the meantime Sharps was on the cusp of significant operating leverage as a large part of their revenue growth from increased route density and opioid disposal kiosks would fall to the bottom line and the market would begin to give credit to the company for its future growth opportunities in the form of a higher stock price. As the value of our portfolio began to deteriorate significantly in March, the SMED stock surged to over \$6.00 and as the position was over 20% of the overall portfolio, we took half of it off the table and added to our other positions. With the price continuing to surge past \$7.00, or a 100% return in less than two years, and knowing the tendency of microcap stocks to “round trip”, we decided to book the profits for this position via a fortuitously available block sale at \$7.00 as we were skeptical at the company’s ability to live up to its valuation in the near term. If the price does indeed roundtrip we will be more than happy to buy back in as we like the management team and the opportunity set.
- Altria Group (MO) – We made an 9% Core Portfolio investment in Altria group at sub \$40.00 in 2019 with the view that it was a good place to park cash at an 8%+ dividend yield with liquidity and a 15-25% annual IRR upside. When the stock reached \$50+ in early 2020 we took half of our position off the table and took the rest off back at \$40 in the spring 2020 as we are positioning our portfolio to have significantly higher upside in the nanocap space as the economy and the small cap markets recover over the next few years. We may come back to MO in the future as it is a solid dividend yielding investment, but as we mentioned earlier, our strategy does involve off-the-beaten-path

companies with an opportunity to get repriced on growth of revenues and earnings and Altria Group's low growth was not going to get us the returns we seek given the repricing of the value segment of the small cap markets.

Enhanced Portfolio Sales

- Rosehill Resources Warrants and Units (ROSEU/ROSEW) – In early 2018 we added a ~4% position in the units and warrants of a nanocap E&P company. As we had some asset inflows in 2018 and 2019 we decided not to add to the position and through 2018 it held steady as a 2.1% position (as was by anticipated design) where we felt the risk and reward were at an appropriate sizing for the portfolio. A combination of leverage and a declining energy markets in 2019 and a significant appreciation of our portfolio in 2019 led this position to be permanently impaired at a little over 10 basis points of the overall portfolio and we were holding the position as a potential capital loss tax offset against a future capital gain recognition in something like a Sharp's Compliance situation described above. We were fully expecting the company, whose stock and unit price were trading at sub \$1.00 relative to \$8+ unit purchase price, to declare bankruptcy and not survive the energy market crash of 2020 which is essentially what happened in July 2020. Much to our surprise in the middle of June 2020 the ROSEU instruments went from an average price of \$0.50 and average daily volume of a few hundred shares to over \$7.00 on hundreds of thousands of shares of daily volume. Since the units were just a combination of the stock (\$0.50) and warrants (\$0.05), whose prices remained relatively flat, the price and volume action were indicative of the broken pricing mechanism in current markets as this was clear it was just computers trading a stock instrument with each other without any regard to the fundamentals of the underlying company or instruments. We happily took the opportunity to get rid of our position at close to \$4.00 before (as well as the warrants, to offset the aforementioned SMED gains) before the price came back down \$0.50 in the following days.

Core Portfolio Additions

- Currency Exchange International (CURN/CXI) - We added a 8% Core Portfolio position in the US shares of the \$50mm market cap foreign currency transaction processor in the 2nd quarter of 2020 at prices between \$8 and \$9 per share. This is an interesting company that currently has ~\$70mm in net cash on its balance sheet (i.e. a negative enterprise value of about \$20mm) that provides retail currency exchange services through its 43 agent locations in US and Canada as well as a fast growing wholesale banknote and foreign currency exchange business for banks and enterprises on its software platform. We were thoroughly impressed with the CEO, founder and significant owner, Randolph Penna, who previously (and not unlike our investment in Research Solutions and its CEO and founder Peter Derycz) has founded a similar company in the past, sold it to a bigger competitor (Bank of Ireland); successfully ran the operations for many years, bought back the retail operations during the financial crisis and after the expiration of the non-compete built a much better wholesale software solution with the same team (that notably has been with him for over 10 years or more).

There are a few interesting aspects to this company that made close to \$6mm in Free Cash Flow last year, and we believe was on track to print a double digit FCF number in 2020 before the Covid pandemic shut down the global travel economy, likely causing it to burn \$4-5mm this year instead. The company grows its business through both sides: retail which tends to be a source of foreign exchange and wholesale which tends to use it. Keeping both sides in balance lowers its own currency transaction costs and more notably becoming a Class 1 registered entity in the US this year will allow it to save significant costs by sourcing its currency directly from the Treasury. The other interesting, somewhat event driven dynamic, is the opportunity to take market share from its main competitor

Traveler that has had significant financial and fraud problems in 2020. This is not unlike the Moneygram situation during the financial crisis that lost significant share after blowing up its book with considerable mortgage backed security (MBS) investments. As CURN is currently close to \$30mm overcapitalized we believe there is significant opportunity for an experienced management team to pick up share through strategic transactions and customer acquisition.

We believe with the development and high growth of use of its software platform that focuses on flexibility and ease of use by its customers by providing turnkey solutions and aligned interests and with an eventual return of global travel in 2021/2022 Currency Exchange International can quickly go from a balance sheet story to a high multiple fintech situation with triple digit returns from today's levels. We would like to make this a bigger investment, at closer to 10% of the portfolio but for now we are comfortable with our sizing as we wait and see how the company navigates the tumultuous economic and competitive waters.

- We have been patiently adding to, currently at 5%, Core Portfolio position in a microcap chemical company for the last year. This is somewhat an illiquid security that has had large price swings so we have been trying to be as patient as possible in adding at the lows to make sure our average cost is at our estimate of the balance sheet. We believe this cyclical company has a really good opportunity to participate in the global economic recovery and we look forward to updating you on the position once we have completed our purchase, though of course you can call us to discuss at your convenience.

Enhanced Portfolio Additions

- US Global Investors (GROW) - We added a 4% position in the stock (3.5%) and short term options (.5%) of a US based asset manager that manages the JETS, an airline focused, ETF that grew its assets under management (AUM) in the 2nd quarter of 2020 from less than \$100mm to an average of \$1.2b. This is a tiny company whose market value at our mid \$2s purchase price was about \$37mm and with ~\$14mm in cash and marketable securities its enterprise value was close to \$20mm. Last year company had close to \$5mm in revenues in managing their funds and ETFs, but an additional \$1.1-\$1.2b in 60bp management fees can add close to \$7mm in additional revenues to the top line i.e. over a 100% growth. The company also owns a gold-oriented ETF that grew its assets from \$50mm to \$125mm so far this year, likely resulting in another \$0.5mm revenue run rate addition. This is not meant to be a long term hold position and frankly we are not sure whether management is going to pay themselves most of the additional gross profits but we believe there is a high probability of the market adjusting accordingly once the revenue growth numbers are reported in the 2nd half of 2020. This is a small position that is meant to be a bet on owning the casino of today's gambler-oriented market rather than participating in the casino itself.

Other Portfolio Updates

- Research Solutions (RSSS) – Research Solutions continues to remain our biggest and highest conviction holding at close to 15% of the portfolio, its size mostly as a function of holding somewhat steady while the rest of the portfolio participated in the draw down during the spring. The company's synergetic segments, Transactions and Platforms, continued to grow above their trendlines at 6% and 34% in the first quarter of the year, with the recurring revenue Platforms component growing at 39%. The main part of our core thesis, that the growth of the Article Galaxy platform would be the significant driver of growth in revenues and profits, continues to bear out as the company recorded a record annual recurring revenue number at \$4.1mm with 374 subscriptions and signaled that its experiencing

significant momentum in growth of Platforms. As we discussed previously, what makes stocks go up is growth in revenues and profits. For the last few years RSSS has used the \$5-6mm in operating earnings from its slow growing and 22-23% gross margin Transactions business to invest in R&D and SG&A of its high growth and 82-83% gross margin Platforms business. During this period, the company's combined \$8 to \$9mm in gross profits were used to cover its \$8-9mm in fixed SG&A and R&D expenses while continuing to lower its losses every quarter, reaching breakeven this year. We have high confidence that the company is at the end stages of growing out its fixed cost base, having filled out its sales suite in the last year and in the early stages of high growth in the Platforms segment, with the expectation that each additional revenue dollar will fall to the operating earnings line and will grow in high double digits for the foreseeable future.

This is a clear example of the operating leverage concept we discussed earlier where the market underestimates the earning power of a business model, especially in under-covered small capitalization companies, until the earnings and the recurring revenue nature of the business model begin to show up in results. So where do we see this company going from here? On the downside its steady cash flowing Transactions business, which notably would have lower growth without the Platforms segment, and the \$8mm in net cash on the balance sheet continue to provide good downside protection at today's stock price and \$60mm market capitalization. On the other hand, there is significant opportunity to penetrate the 700,000 corporate and academic research organization market. With Covid keeping most workers at home, this has provided a bigger opportunity for the company to demo its product in addition to increased interest in streamlining the R&D processes of research organizations. We believe that even keeping on the current revenue growth trendlines should result in significant profitability for the company with an eventual re-rating to their information services peers such as CoStar or Verisk Analytics, with similar strong defensible moats, resulting in many multiples from today's price.

Unfortunately, as is usually the case in closely held nanocap stocks with significant insider ownership, even small moves in changes of holdings of their biggest owners, can create stock moves contrary to the company's fundamental moves. When we originally invested in RSSS it was an Over The Counter (OTC) stock with barely a thousand shares a day traded and it had taken us over a year to slowly build up our position in the stock between \$1.00 and \$2.00 per share. In order for the stock to be more investable for institutional investors it needed to get uplisted to Nasdaq by adding only a couple of more million dollars to its book value equity cushion. While the company would have reached this milestone organically within a year by growing its earnings, its largest shareholder helped to speed the process along by converting their warrant position in the 1st quarter of 2020 and adding almost 2mm more shares to their already large, 25%+, holding which understandably they needed to reduce. These actions and seemingly forced liquidation by another large shareholder caused the stock price to drop over 20% in the 2nd quarter, accounting for a large part of our partnership's negative returns in the quarter. While unfortunate in its timing, we strongly believe the aforementioned stock dynamics are temporary and should reverse as the company continues to deliver on our thesis.

- Acorn Energy (ACFN) – Acorn remains our smallest capitalization holding at around \$8mm in market capitalization and \$6mm in enterprise value, with ~\$1.9mm in next cash on the balance sheet and represents approximately 8% of the portfolio today. During the March sell off it experienced a 50% decline in its very illiquid stock price and has not bounced back despite balance sheet value with the aforementioned cash, net working capital and \$70mm of Net Operating Losses (NOL) value held at the Acorn Energy holding company level. Much like the majority of our holdings, our bet on Acorn has to do with the operating leverage potential of its 99% owned subsidiary OmniMetrix that

specializes in hardware sales and monitoring services that prevent an average of a 10% failure rate for back up energy generators, pipeline corrosion systems, and air compressors.

What makes OmniMetrix incredibly valuable is its fast growing, high margin \$3.6mm in annualized recurring monitoring revenues (ARR). The company has over 25,000 generator monitoring subscription users paying over \$120 a year at 80%+ gross margins for its services and with a 90%+ retention rate the customers stay with the company for well over 5 years. The company grows its ARR through hardware sales via the independent generator dealer network at an average of \$400,000 to \$800,000 per quarter, where for every \$100 in hardware revenues, on average, creates an additional sticky \$60+ in ARR. In other words, for every additional hardware revenue dollar over a \$100,000/quarter the company grows its ARR base, including 17% in 1Q 2020. While it is hard to predict today the path of the quarterly revenues on a short term basis, we have high confidence in the company's CEO and significant shareholder Jan Loeb to continue to successfully grow the ARR base to over \$7.5mm in the next few years given the attractive economics of the aforementioned growth model and given the fully built out fixed cost SG&A base, not unlike our Research Solutions situation above, we expect the significant flow through to fall to the bottom line in the form of tax shielded Free Cash Flow at \$2-3mm a year for the OmniMetrix subsidiary, from breakeven today. The real problem continues to remain that the company, with \$800,000+ public company corporate costs, should not remain a public company and is likely much more valuable in the hands of an industrial strategic acquirer with a larger sales force and elimination of public company costs, a situation that we expect to play out at multiples of quarter end's \$0.22 stock price, within our multi-year holding period time frame.

- Shyft Group/formerly Spartan Motors (SHYF) – Our 10% Core Portfolio holding in the leader in the fleet vehicle manufacturing market has performed relatively well this year, down approximately 20% through the end of the 2nd quarter and relatively flat for the year as of the writing of this letter, despite being down over 50% in March. Despite the tumultuous economic environment the company has continued to perform well in the 1st quarter, grew its fleet vehicle segment (FVS) backlog 187% to over \$300mm and made a number of value creating strategic M&A moves over the last year.

When we originally invested in Spartan, the company consisted of three segments: FVS, Specialty Vehicles, and Emergency Response. While the former two segments have been good performers, the ER segment, despite significant efforts by the management team, was a persistent drag on performance and continuously under earned its cost of capital, barely getting above breakeven in decent economic environment. In late 2019 the company purchased Royal Truck Body, a California based manufacturer of specialty truck bodies for a net, of tax benefits, purchase price of \$80mm that immediately strengthened its SV segment with significantly beefed up geographic distribution and higher margin products. Additionally, the company continued to increase its market share in the Class A Diesel Luxury Coach Market to 28% (from 26%) despite the market being down 8% in 2019. On the other hand, the ER segment just could not catch any traction over the years since we have held this investment and in 1st quarter of 2020 the company sold the segment and the Spartan Motors brand for \$55mm to Rev Group.

While the sale price tag was not amazing, the two transactions transformed the company profile to a strong double-digit growth and Cash Flow Return On Assets earner. Additionally, this made Shyft Group more of a pure play on the secular theme of the “last mile delivery” industry, one that has seen parcel delivery more than double in the last four years. The package volume is expected to continue to grow at or above its 19% CAGR trend for the foreseeable future as e-commerce enjoys both secular and Covid-related tailwinds and take more share from retail sales, still at a surprisingly low 16% today.

While there may be more near term logistical challenges, not unlike what we saw in the 2nd half of 2018, we believe the company is well on its way to over a \$100mm in EBIT over the next few years, a good proxy for cash flow, from our estimate of ~\$50mm this year, as the lower capital intensity and higher volume throughput should translate into a significantly more powerful operating leverage flow through to the bottom line. While we added to the stock at the March 2020 lows, we had to reduce our position back down to 10% of the portfolio on our portfolio risk management process, though we still continue to believe the company can deliver triple digit returns from today's price levels on growth in earnings and higher multiples reserved for growth companies.

- Flotek (FTK) – Flotek continues to be a significant part of our Core Portfolio, whose representation changes from 8% to 14% as its price recovered to over a 150% from its March 2020 lows. Our original thesis on the stock was that the company, that at one point was trading at 30% to its liquid balance sheet values of cash and Net Working Capital, had an incentivized board that would force significant value creation via stock buybacks or outright liquidation. In fact, given the significant energy market implosion in the spring of 2020, we felt our thesis was much likelier to come to fruition as it was apparent that the rig count based business model into which the company sells its enhanced oil well recovery chemicals was unlikely to come back. We were initially somewhat dismayed that the company opted to hire John Gibson Jr, one of the most respected industry veterans, as CEO and Chairman of The Board instead and focus the strategy on using the \$100mm+ cash pile to acquire more companies, which at the time we felt was an imprudent use of capital. However, as we have had the opportunity to have numerous conversations with Mr. Gibson and to hear his strategy and thought process, as well as learn about his background and watch him quickly make value creating moves we have decided to stick with our investment albeit at a changed thesis.

Mr. Gibson Jr, quickly recognizing that the old business model is dead on arrival and the volumes of the past were not coming back, renegotiated the supply agreement, based on old volume projections, with Archer Daniels Midland that bought the company's Florida Chemical division, for an up front payment of \$15mm that significantly reduced a much higher cash burn had the agreement remained in place. Soon after the company made a splash by purchasing JP3 Measurement for \$36.5mm for a combination of balance sheet cash and shares. JP3's product is a measurement technology that allows for operators to obtain real-time (< 30 seconds) data on the composition and physical properties of hydrocarbons across a variety of upstream, midstream, downstream, and distribution use cases. The data is predominately used by operators to assist in process optimization efforts and boasts a diverse range of applications. The company has grown impressively in 2019 with only 3 full time sales staff and despite an upstream market pullback by focusing on the downstream market, including a milestone deal with Phillips 66, a deal we strongly suspect was brought together by Mr. Gibson himself.

So where does that leave us today? While the stock price has surged in July 2020 close to our cost basis and significantly above our spring 2020 additions, the company, at a \$110mm valuation still has, by our estimates, \$70mm in cash and \$10-20mm in other liquid assets. The legacy chemicals business whose \$80mm revenue run rate that is 50% below its peak, is likely to shrink even further and we envision it being significantly smaller but with higher gross margins and longer term contracts, with the worst case scenario the entire division being sold for patent value and/or a years worth of gross profit value in the \$10-20mm range. There is of course the optionality that oil comes back and the division grows and penetrates the less rig count dependent Enhanced Oil Recovery market segment enough to have a viable economic value again but for now we believe it is priced as a free option within the business. So our real investment here, at the balance sheet price, for the ability of a very

incentivized and experienced CEO and Board to grow the JP3 business into its \$1b Data As A Service (DaaS) Total Addressable Market (TAM), from ~\$14mm in revenues last year, with already significant hires on the business development team and with more on the way, using the CEOs extensive network to strike Phillips 66 type deals. We also expect one or two more JP3-like deals on the way to completely transform the company from an old school chemicals provider to a more high growth energy tech firm with high growth and recurring revenues. With the market still not pricing the stock above its balance sheet values, we believe the JP3 business could be worth more than double the stock price today and with significant optionality on the recovery of the chemicals business and additional successful deal wins. We are excited to see what happens from here over the next few years and feel comfortable with our downside and upsides from here to keep Flotek as one of the top positions in the portfolio.

- Gaia (GAIA) – Our investment in GAIA continues to remain one of our largest holdings at close to 14% and for good reason. While the stock has mostly stayed flat this year (though with a major decline in March and a subsequent rebound) the business continues to deliver on our thesis on all cylinders. In late 2018 the company pivoted from being a “high growth regardless of costs” story, which ironically are the most sought after stocks in the market today, to one of slower revenue growth, from 60% to 20% a year, but one that was focused on reaching Free Cash Flow generation by June 30th, 2020 without needing to access the capital markets. Since 3rd quarter 2018, or a little over a year and a half to end of June, 2020, the company has grown its subscribers 43% to 664,000 and quarterly revenues to over 50%, at \$16.2mm, on the back of strategic price increases, while cutting the Operating Cash Flow loss \$8.4mm a quarter to \$1.9mm in profit at the end of June. In middle of June the company updated the market on reaching its 650,000th subscriber and achieving sustainable Free Cash Flow profitability and in August of 2020 the company reported a 664,000 subscriber number as the churn continued to improve.

With Covid-19 changing both, the ways the public exercises and increasing the volume of entertainment consumption, we believe Gaia is in an excellent position to capitalize on these trends with a significant customer base and brand name, as well as substantially lower customer acquisition costs (CACs). CACs have benefited from having the high churn rate vintages from 2017 and 2018 no longer being part of the net CAC cost base as well as lower rates from the typical customer acquisition channels as the economic slowdown takes its toll on the advertising rates. We believe with the quarterly CACs and corporate expense costs staying relatively flat for the last year, while the company continues to both, grow its subscriber base and raise prices on its formerly grandfathered accounts we should begin to see the power of the operating leverage inherent in the business model as a significant part of the new revenues should fall to the bottom line as Free Cash Flow. Our expectation that by 2021 we should see EBITDA/Free Cash Flow at above \$20mm and \$14mm with the market beginning to appreciate the earning power of the \$150mm market capitalization company by the end of 2020, re-rating it to high double digit EBITDA and high single digit revenue multiples of its streaming peers to a stock price multiples higher than it is today.

- HireQuest (HQI) – We continue to hold a significant Core Portfolio position in HireQuest, at above 13% of the portfolio, as the company’s stock held up admirably in 2020, down a little over 10% in the first half of the year. Our thesis remains unchanged and largely on track, with HireQuest, the larger acquiring entity through a reverse merger in 2019, acquiring approximately 20 owned branches from Command Center, the public company. Through sales and franchise agreements over the last year HireQuest converted the branches into franchises where at the end of March 2020 it managed 135 staffing franchises throughout the United States.

Of course, owning a staffing business in the middle of pandemic will have certain moving parts and having a number of branches closed and not generating franchise fees in the spring is unlikely to result in growth this year. However, the dynamic of having a working capital intensive franchisor business during the slowdown results in significant cash cycle release, where in the 1st quarter the \$75mm market cap company generated \$5.5mm in operating cash flow adding to its \$4.5mm cash balance. We expect an additional \$5-10mm in cash flow generation this year from both, ongoing operations of franchisee fees and notes receivable interest, and more working capital releases. Of course we'd rather see growth in the topline but given the recessionary environment building up a significant cash balance is likely to allow the company and its 44% owner and founder CEO Rick Hermanns to be strategically opportunistic. In fact, in June 2020 the company whose 68% of the shares are owned by insiders, and averages 6,600 daily average announced a 1mm share, or 7.5% of outstanding shares, buyback. The bigger number however is that this buyback represents close to 25% of the float, and we'll be looking forward to seeing the execution of this buyback. In the meantime, the CEO and the board have made 116 insider purchases on the open market in 2020 giving us somewhat of an increased confidence level.

Its hard to predict where this company will end in 2020 with parts of the economy like hospitality essentially shut down, while other parts like homebuilding surging, however, we expect the company to continue to generate positive, ex working capital release, earnings and cash flows in 2020. Looking a few years out, with the transition to an all franchise model and a likely return of positive economic growth in late 2021/early 2022 we can see the company generating a growing \$10mm+ a year in Earnings Before Interest & Taxes (EBIT) / Free Cash Flow (FCF) at 60%+ operating margins and returning this cash to shareholders via more buybacks and dividends with our intermediate term price target at above \$10/share.

- Recro Pharma (REPH) – Recro is our other Core Portfolio significant underperformer, down over 70% from its year end 2019 peak, when we took close to two thirds of our gains off the table both on the Recro Pharma position and Baudax Bio spin-off. Nevertheless, the position remained at 10% size at the beginning of the year and its decline to approximately 30% below our cost average certainly hurt. So what caused the standard microcap roundtrip? This was essentially the case of the management not managing the market expectations. In 2019 the company grew the topline 28.5% to almost a \$100mm and operating income to \$32.3mm on the back of a significant competitor, Mylan, being out of the market for most of the year where Recro was able to pick up most of the market share for one of its key product lines. As 2020 began the company was caught flatfooted as Mylan came back to the market with 50% market share and two of the company's customers discontinuing their product lines with a \$4mm negative revenue impact in 2020 and \$7-8mm in 2021. With the market expecting a close to \$60mm EBITDA number in 2020, a subsequent guide down to a sub \$30mm, and \$80mm to \$85mm in revenues, in February and May destroyed the management's credibility over their ability to forecast their business and the stock is likely to be in a timeout for most of 2020.

With the stock down to low \$4.00/per share range and a sub \$100mm market capitalization and a now, somewhat dangerous, \$90mm in debt, this now 6.0% Core Portfolio position, is likely to become a source of cash in the portfolio. We no longer expect a \$20+ sale and are concerned that there may be more product revenue decline announcements in the future. However, we believe the company's likely longer term \$80mm revenue and a \$10mm/\$35mm EBIT/EBITDA run rates along with significant manufacturing capacity during a secular move to bring onshore drug manufacturing back to United States is worth more than the current \$4.15 per share price and while this position is on its way out we will be patient with our exit strategy.

- US Ecology October 2023 \$58.67 Warrants (ECOLW) – Our 6% Enhanced Portfolio position in the post-merger, converted warrants of NRCG group, has also been a significant underperformer as the US Ecology stock has not yet recovered from a March 2020 sell off. This is an economically sensitive holding of a diversified specialty waste management company with a significant number of valuable assets including the fast growing Standby Services segment acquired from NRCG. While one of our marginal process improvements is to lower the portfolio allocation to Enhanced Portfolio from an average of 20% to 10% or less, the US Ecology warrants continue to be an extremely high conviction investment for us.

We consider the US Ecology collection of waste disposal assets and services, 80% recurring revenue base and a highly diversified blue chip customer list, to be highly underappreciated by the market. The jewel of the business, the Environmental Services business segment at over 65% of revenues sports 40% operating margins and grew over 20% in the first quarter. The challenge in 2020, brought on by Covid, has been the decimation of the energy sector which accounted for 12% of revenues, including two brand new, NRCG built, Eagle Ford and Permian landfills, clearly impaired by the energy market challenges as well as a slow down in some industrial services. While this year will be one of digestion of Covid-related events and the NRCG merger, and will likely come in at \$180-\$190mm in EBITDA we strongly believe that the company can reach a \$240mm - \$250mm EBITDA run rate within the next two years on organic growth and an economic recovery where a current 10x to, an industry median, 13x, EBITDA multiples would result in \$70 to \$90 stock prices, significantly above the \$58 warrant strike price resulting in 3x to 7x returns from today's warrant prices. Finally, while the economic challenges put the company into cash conservation mode, with a suspension of a dividend and \$70mm in cost cuts, with the warrants representing over 10% dilution for the company it is still likely an opportunistic and shareholder value oriented management team would look to tender the warrants prior to an eventual stock rebound.

This has been a tough first half of the year in the markets, but one that is not reflecting the economic reality both from the small capitalization value side and one from high growth tech side. Financial theory dictates that a company's valuation is a function of its cost of capital and growth and with the cost of capital at historically unprecedented lows most of the focus tends to fall on growth, where companies even with what in the past was considered great growth will be relegated to the lowest quintiles of market valuation segments. The gap between growth and value factors for indexes of all capitalizations has continued to get wider, and will be unlikely to ever close all the way given the semi-permanent nature of low interest rates. However, as our quote in the beginning of the letter dictates this is not the first or the last time where the markets exhibited extreme irrationality and euphoria disconnected from reality. The late 90s come to mind, with the Asian financial crash followed by a few more years of euphoric tech led market leadership and the return of value. Of course, if we look further back, through the 70s and 80s we can find similar periods, though of course with different underlying dynamics. So, while it may seem that things are dire in microcap value land, we continue to be very confident in our process and our mandate. We have 9 companies in our Core Portfolio with a median market cap of \$80mm and median enterprise values close \$65mm with over 70% of the portfolio expecting to have positive growth in 2020 creating operating leverage inflection points that we expect will result in a substantial re-rating of our portfolio in the near future that we have already begun to see in the 3rd quarter of 2020.

Subsequent Events

As of the publication of this letter, in the first week of August 2020, our portfolio appreciated approximately 20% of its June 2020 quarter end lows. While we generally do not like to publish mid period updates, given the volatility and the unfortunate timing of the quarter end values we felt it would be important to have this mid period update that better reflects our portfolio value today.

Next Fund Opening

Our next partnership openings will be September 1, 2020. Please reach out for updated offering documents and presentations at info@artkocapital.com or 415.531.2699.



Appendix A: Performance Statistics Table

	Artko LP Gross	Artko LP Net	Russell 2000 Index	Russell MicroCap Index	S&P 500 Index
YTD	-44.4%	-44.5%	-13.0%	-11.2%	-3.1%
1 Year	-26.0%	-29.6%	-6.6%	-4.8%	7.5%
3 Year	-5.2%	-8.3%	2.0%	0.9%	10.7%
Inception 7/1/2015	37.1%	12.0%	23.4%	15.1%	66.6%
Inception Annualized	6.5%	2.3%	4.3%	2.9%	10.7%
Monthly Average	0.7%	0.4%	0.5%	0.4%	0.9%
Monthly St Deviation	6.4%	6.0%	5.8%	6.2%	4.2%
Correlation w Net	-	1.00	0.76	0.73	0.70



Legal Disclosure

The Partnership's performance is based on operations during a period of general market growth and extraordinary market volatility during part of the period, and is not necessarily indicative of results the Partnership may achieve in the future. In addition, the results are based on the periods as a whole, but results for individual months or quarters within each period have been more favorable or less favorable than the average, as the case may be. The foregoing data have been prepared by the General Partner and have not been compiled, reviewed or audited by an independent accountant and non-year end results are subject to adjustment.

The results portrayed are for an investor since inception in the Partnership and the results reflect the reinvestment of dividends and other earnings and the deduction of costs, the management fees charged to the Partnership and a pro forma reduction of the General Partner's special profit allocation, if applicable. The General Partner believes that the comparison of Partnership performance to any single market index is inappropriate. The Partnership's portfolio may contain options and other derivative securities, fixed income investments, may include short sales of securities and margin trading and is not as diversified as the indices, shown. The Standard & Poor's 500 Index contains 500 industrial, transportation, utility and financial companies and is generally representative of the large capitalization US stock market. The Russell 2000 Index is comprised of the smallest 2000 companies in the Russell 3000 Index and is generally representative of the small capitalization U.S. stock market. The Russell Microcap Index is comprised of the smallest 1,000 securities in the Russell 2000 Index plus the next 1,000 securities (traded on national exchanges). The Russell Microcap is generally representative of the microcap segment of the U.S. stock market. All of the indices are unmanaged, market weighted and reflect the reinvestment of dividends. Due to the differences among the Partnership's portfolio and the performance of the equity market indices shown above, however, the General Partner cautions potential investors that no such index is directly comparable to the investment strategy of the Partnership.

While the General Partner believes that to date the Partnership has been managed with an investment philosophy and methodology similar to that described in the Partnership's Offering Circular and to that which will be used to manage the Partnership in the future, future investments will be made under different economic conditions and in different securities. Further, the performance discussed herein does not reflect the General Partner's performance in all different economic cycles. It should not be assumed that investors will experience returns in the future, if any, comparable to those discussed above. The information given above is historic and should not be taken as any indication of future performance. It should not be assumed that recommendations made in the future will be profitable, or will equal, the performance of the securities discussed in this material. Upon request, the General Partner will provide to you a list of all the recommendations made by it within the past year.

This document is not intended as and does not constitute an offer to sell any securities to any person or a solicitation of any person of any offer to purchase any securities. Such an offer or solicitation can only be made by the confidential Offering Circular of the Partnership. This information omits most of the information material to a decision whether to invest in the Partnership. No person should rely on any information in this document, but should rely exclusively on the Offering Circular in considering whether to invest in the Partnership.