Old West Investment Management, LLC

July 12, 2018

Dear Investor,

The first half of 2018 was marked by a sudden end to investor complacency in early February, but the following four months saw markets return to positive returns and investor optimism. As you can see in your enclosed statement, we had an outstanding second quarter and first half the year.

So where do we go from here? That, as they say, is the $64,000 question. There is much to be optimistic about and alternatively much to be concerned about. The U.S. economy has greatly benefited from the Trump Administrations tax cuts and ongoing elimination of burdensome regulations. Second quarter GDP very well could come in at 4%, and with unemployment running at plus or minus 4%, these are definitely good times for many Americans.

On the other hand, this bull market has run for 9 ½ years, the second longest run in post-war history. What could bring it to an end? There are many possibilities, both known and unknown. The FED continues on its track of "quantitative tightening," where they are slowly unwinding their $4.5 trillion portfolio of bonds. For the past eight years they have been competing in the open market buying bonds (with dollars printed out of thin air), and artificially suppressing interest rates. This has created an easy and cheap money environment that has created record high prices in the stock market, bond market, real estate and collectibles. With the economy on solid footing the FED has no choice but to begin tightening. They will do this by continuing to raise the federal funds rate and steadily liquidate their massive stockpile of bonds. Now the FED is competing in the open market to sell bonds, along with the U.S. Treasury to finance our $1 trillion annual budget deficit, and every state, county, city and town most all operating in the red. This deluge of bonds being sold will create an over supply situation which will lead to lower prices and higher interest rates. The ten year US Treasury bond has doubled in yield since rates bottomed two years ago this summer, which was the end of a 35 year cycle of interest rates falling.

Our current trade battles with the rest of the world are creating uncertainty, but I believe Trump knows exactly what he's doing. His real battle is with China, not Europe or our North American neighbors. As I have written in many of my past letters, China has a debt bubble where they have no way out. Their banking system has exploded to over $40 trillion, and that amount is riddled with bad debt. At the same time, the Chinese are becoming increasingly bold in their imperialistic ambition. Building islands with military bases in international waters does not set well in Washington. We export $115 billion of goods to China each year, and we import $580 billion from them. They clearly need us much more than we need them. I believe Trump, a master negotiator, will be able to extract many concessions from the Chinese.

Another threat to the markets and economic growth, is the explosion of debt worldwide. Global debt has grown to $240 trillion, an all time high. As interest rates continue to rise, the servicing of this debt will become increasingly burdensome. This is not conducive to growth and prosperity.

Taking all these facts into consideration, we at Old West are increasingly defensive with your money, and we feel we are well positioned for whatever Mr. Market might throw at us. Job one is to preserve and smartly grow your capital, and job two is not to forget job one.

Update on Cheniere Energy (LNG)

I wrote to you about Cheniere two years ago this month. I wanted to give you an update on the company because it's one of the greatest success stories in American energy that I've ever seen. Cheniere, whose stock symbol is aptly LNG (liquified natural gas), has revolutionized the U.S. natural gas industry.

Cheniere has two locations, Sabine Pass, LA, and Corpus Christi, TX. At each of these locations they operate what they call "trains" where they receive natural gas by pipeline, go through a process to chill the gas to -240°F, a temperature that transforms the vapor to liquid compressing its volume 600 times. It's shipped by vessel all over the world, and upon arrival its deliquefied for use. Cheniere is building six trains at Sabine and three at Corpus. At the time of my last writing they were operating three trains. Within two years they will be operating all nine trains. Here are the numbers:

	2016	2020 Est.
Revenue	$1.3B	$10.2B
Net Profit	$-480M	$1.3B
E.P.S.	$-2.10	$3.64
Free Cash Flow	$-4.7B	$1.45B
Production	14M tons/year	40M tons/year

The beauty of the Sabine and Corpus locations is both are strategically located near some of the biggest natural gas fields in the US. Cheniere has 1,000 acre properties at both locations, both situated on the Gulf of Mexico. The average cost of our Cheniere shares is $34. It is currently trading at $63 per share. As you can see on the above chart, once all nine trains are operating, the company will gush cash flow and profit for years to come.

One aspect of Cheniere's business model that I love is they don't bear commodity market risk. The vast majority of production is contracted to major international users of natural gas like British Gas, Femosa of Spain, Korea Gas, Gail India, Total of France, Centrica of U.K., Pertamina of Indonesia, and of course China. Cheniere is paid a fixed fee to liquify and ship the gas, and the customer is playing the natural gas market. Some of Asia's smaller economies like the Philippines, Sri Lanka, Bangladesh, Pakistan, and Vietnam are also beginning to receive LNG. Pakistan is currently a small buyer of LNG, importing 4.5M tons per year, but it is planning to expand to 30M tons by 2022.

Every country in the world wants to decrease or eliminate coal as a fuel source for the production of electricity. Coal fueled power plants are the number one source of air pollution in the world. Alternative methods of electricity production would be solar, wind, and nuclear (all completely clean), and although natural gas is not completely clean, it is much cleaner than coal. Wind, solar, and nuclear all have obvious limitations, whereas natural gas is cheap, abundant and widely used.

Cheniere brought in a new CEO, Jack Fusco, two years ago and he has done a great job of streamlining the company and minimizing expenses. Last year President Trump invited Fusco on an international trade mission, and Trump is a big booster of American energy production and independence, and he sees the exporting of natural gas as a growth industry for years to come.

We are thrilled with our investment in Cheniere energy, and we expect it to be a long term compounder in our portfolio for years to come. We look forward to the second half of the year, and we are thankful for your loyal support.

Sincerely,

Joseph Boskovich, Sr.
Chairman and Chief Investment Officer