January 15, 2018

Dear Investor:

The year 2017 will long be remembered as one of the most surprising years in stock market history. Surprising because of the extreme skepticism surrounding the election of Donald J. Trump as the 45th President of the United States and the ensuing market run. I was watching the election results live when the New York Times (much to their dismay) declared Trump the winner and stock market futures quickly plummeted 300 points. Once investors realized that the world was not coming to an end with The Donald as president, the market recovered and actually closed higher the next day.

At the time of the election, the market had risen for eight years since the end of the recession, and by any measure the market was not cheap. Nobody predicted the market would gain 21% in 2017, with the tech driven NASDAQ up 30%. At Old West we entered 2017 cautious and defensive and that caused us to underperform the market by a wide margin as you can see on your enclosed statement. Listed below are our top ten holdings with their 2017 performance.

#	Company	2017 Stock Performance
1	Barrick Gold Corp	-9.4%
2	Abbott Laboratories	48.6%
3	New Gold Inc	-6.0%
4	PBF Energy Inc	27.2%
5	Cameco Corp	-11.8%
6	Cheniere Energy Inc	30.0%
7	Chesapeake Energy Corp	-43.6%
8	Fairfax Financial Holdings	9.0%
9	Goldcorp Inc	-6.1%
10	IDW Media Holdings Inc	-8.0%

As you can see Chesapeake Energy and our gold miner holdings were our biggest detractors to our performance. I predict these same companies will be some of our best performers in 2018. I have no idea what the market will do in the coming year, but I can tell you the market is extremely expensive by any measure. Only twice before has the market been this expensive, 1929 and 2000. Never before have all asset classes been at record highs. The stock market, bond market, real estate, art and other collectibles and cryptocurrencies are all at or near record highs. I am old enough and barely wise enough to know that these markets cannot continue going up indefinitely. A correction is coming and possibly a sharp correction. When? I don't know, but we are first and foremost concerned with preserving your hard earned money, not chasing bitcoin and FANG stocks.

There is certainly a lot to like about today's economy and the outlook for company profits. The Trump administration's relentless attack on reducing burdensome regulations on companies is a boon to corporate profits. The new tax law is a godsend to the majority of corporations, and although there were winners and losers with the new bill, corporate America was a clear winner.

President Trump has said U.S. infrastructure will be his top priority in 2018 and that too will be a big plus for American manufacturers of equipment and materials. So there is a lot to be optimistic about, but I believe most of these factors are why the market is at record highs.

Todays markets are priced for perfection, with no regard for potential black swans. What could go wrong that might bring this nine year bull market to an end? There could be any number of "unknown unknowns," but here are three geopolitical trouble spots that are brewing:

1) A hard landing in China. Some experts are calling China the world's largest Ponzi scheme. The Chinese banking system has grown to $37 trillion with the Chinese economy generating $12 trillion of GDP. The Chinese banking system has grown to be twice the size of the U.S. banking system, with an economy half our size. Why has the Chinese banking system grown so large? Because they don't have the financial discipline to write off bad loans, but instead they renew and extend bad loans by the millions. This is unsustainable and the stress in their financial system could result in a crisis. They are big enough to affect the world economy in a way not seen since the Great Depression. This is not a prediction, but a real possibility.
2) War in the Middle East. The tension between Iran with their Shiite allies (Iraq, Yemen, Bahrain, etc.) versus Saudi Arabia and their Sunni allies (Egypt, Syria, Turkey) has been building. Rockets have been fired several times from Yemen towards Riyadh, the Saudi capital, and it is believed Iran is instigating the attacks. Saudi Arabia has a 32 year old prince, Mohammad bin Salman, who has become the emerging leader of the country, and the rhetoric between him and the Iranian leaders has sharply escalated. If war breaks out, I expect Russia will come to the aid of their ally Iran, and that would beg the question what will the US do to assist our ally Saudi Arabia. If Iran and their allies were to get the upper hand in the Middle East, that would put Israel in a very precarious position, which makes our involvement all the more likely.
3) North Korea. Is North Korean leader Kim Jong-un a rational strategic thinker or a narcissistic mentally deranged despot? I don't know the answer nor does anyone else, but imagine the possibilities if it's the latter.

When I say the market is priced for perfection with no regard for potential black swans, none of the three potential crises mentioned above are priced into the market. When buying a stock you need to determine what is a fair price to pay, and we at Old West always want a margin of safety in the price we pay, and that margin of safety needs to include potential geopolitical events. I assure you not many professional money managers are thinking like this today, hence the extreme level of investor complacency throughout financial markets. It is no coincidence that we have significant exposure to gold mining companies, as gold has traditionally been the ultimate flight to safety, which would do very well if any of the aforementioned crises were to occur.

Another challenge for the market in 2018 will be the Fed switching from Quantitative Easing (QE) to Quantitative Tightening (QT). For several years The Fed has been a buyer of treasuries and mortgages backed securities, and this year they have switched to being a seller. They're expected to sell up top $400 billion of their portfolio in 2018. As they begin a multiyear effort to shrink their balance sheet, it will be interesting to see how the equity market reacts to the change.

In all of my quarterly letters I like to highlight one or more of our holdings, and in this letter I will face the music and give you an update on our worst performer last year, Chesapeake Energy.

UPDATE ON CHESAPEAKE ENERGY

Chesapeake Energy (CHK) has been a challenging position for us for several years. We first invested in the company just prior to the collapse in energy prices in mid 2014. We bought it as a turnaround story as the board ousted company founder and CEO Aubrey McClendon. McClendon's ouster was engineered by retired ConocoPhillips CEO Archie Dunham, who came out of retirement to chair CHK's board of directors. Dunham led the search for a new CEO, and the company hired a rising star from Andarko Petroleum, Doug Lawler. Board Chairman Dunham has since purchased $23 million of CHK stock in the open market.

New CEO Lawler inherited a company with a world class collection of oil and gas assets, but he also inherited $20 billion of debt. Lawler immediately realized he needed to sell noncore assets to pay down the debt, and just prior to the collapse of energy price in 2014 he sold 400,000 acres of reserves in the Marcellus Shale to Southwestern Energy for $5.4 billion. The timing of the sale was fortunate, as I doubt CHK would have survived the epic 2014 energy collapse if not for the sale.

Doug Lawler has done a masterful job of saving and resurrecting CHK. He has cut debt from $20 billion to $9.7 billion, he has slashed overhead and expenses, and CHK has become a low cost producer of oil and gas. The company is still the number two producer of natural gas in the U.S., and a top ten producer of oil. CHK today has 11 billion barrels of oil equivalent reserves, 7 million acres and 20,000 wells. They have reserves in South Texas, the Haynesville, Mid-Continent, Marcellus, Utica, and the Powder River Basin.

I visited the company headquarters in Oklahoma City and I was very encouraged to learn they can produce positive cash flow at $50 oil and $2.00 natural gas. The company expects to generate $800 million of net income in 2018.

CHK's stock has traded as high as $26 per share in the past five years and it is currently trading at $4.00. The company is still saddled with the reputation of eccentric founder McClendon and his free spending ways, but now that energy prices have recovered, and Lawler keeps his steady hand on the rudder, you will see Chesapeake Energy become one of the most admired companies in the industry. The stock price will follow.

I am not pleased that we underperformed the market by so much last year. However, I take comfort in knowing that we followed our investment process in owning the companies in our portfolios, and I'm very anxious to see the stock prices of these outstanding companies go much higher in 2018 and beyond. Thank you for your continued loyalty and support, and all of us at Old West wish you and your family a happy and healthy new year.

Sincerely,

Joseph Boskovich, Sr.
Chairman and Chief Investment Officer