SPITFIRE CAPITAL LLC

February 28, 2018

*"The greatest mistake of the individual investor is to think that a market that did well is a good market rather than a more expensive market."*

Ray Dalio, *Reuters*, February 21, 2018

Fourth Quarter 2017

| | Q4 2017 | YTD 2017 | Since Inception |
|---|---|---|---|
| The Spitfire Fund L.P.[1] | +2.7% | +12.4% | +242.7% |
| Russell 2000 | +3.3% | +14.6% | +112.6% |
| S&P 500 | +6.6% | +21.8% | +122.8% |

In the fourth quarter, The Spitfire Fund L.P. (the "Fund") was up +2.7% (net), compared to the Russell 2000 and S&P 500 which were up +3.3% and +6.6%, respectively. For the year, the Fund was up +12.4% (net), compared to the Russell 2000 and S&P 500 which were up +14.6% and +21.8%, respectively. Since inception in July 2007, the Fund has achieved a cumulative net return of +242.7%, representing a compound annual net return of +12.4%. Over the same period, the Russell 2000 and S&P 500 have achieved cumulative total returns of +112.6% and +122.8%, respectively, representing compound annual returns of +7.4% and +7.9%, respectively.

Historical Net Performance Summary

| Year | The Spitfire Fund L.P. | Russell 2000 with Dividends | Relative Performance |
|---|---|---|---|
| 2017 | +12.4% | +14.6% | -2.2% |
| 2016 | +24.0% | +21.2% | +2.8% |
| 2015 | -0.7% | -4.4% | +3.7% |
| 2014 | +6.9% | +4.9% | +2.0% |
| 2013 | +28.9% | +38.8% | -9.9% |
| 2012 | +31.5% | +16.4% | +15.1% |
| 2011 | +3.6% | -4.2% | +7.8% |
| 2010 | +36.6% | +26.8% | +9.8% |
| 2009 | +75.6% | +27.1% | +48.5% |
| 2008 | -39.4% | -33.8% | -5.6% |
| 2007 (partial year) | -9.3% | -7.6% | -1.7% |
| Total Return | +242.7% | +112.6% | +130.1% |
| Annualized Return | +12.4% | +7.4% | +5.0% |

[1] The Spitfire Fund L.P. commenced operations on July 1, 2007. Performance data is through December 31, 2017 and is presented net of all fees and expenses. Index performance is presented on a total return basis assuming reinvestment of dividends.

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For the quarter, the top contributors to performance were GTT Communications, Inc. (NYSE: GTT); Builders FirstSource, Inc. (NASDAQ: BLDR) and Beacon Roofing Supply, Inc. (NASDAQ: BECN). The primary detractors from performance were Horizon Global Corporation (NYSE: HZN); Owens-Illinois, Inc. (NYSE: OI) and Libbey Inc. (NYSE: LBY). For the year, the top contributors to performance were GTT Communications, Inc. (NYSE: GTT); Builders FirstSource, Inc. (NASDAQ: BLDR) and National Research Corporation (NASDAQ: NRCIA). The main detractors from performance were Libbey Inc. (NYSE: LBY); Horizon Global Corporation (NYSE: HZN) and Natural Gas Services Group, Inc. (NYSE: NGS). We ended the year with gross and net long exposure of 83% and cash of 17%, which were also the average exposures for the year.

We did not make any new investments in the fourth quarter. During the year, we added two including US Foods Holding Corporation (NYSE: USFD), a leading domestic foodservice distributor, in the second quarter, and an investment in a U.K. plc in the third. We exited investments in Crawford & Company (NYSE: CRD-A), a claims adjuster and insurance services provider, and in Drew Industries, now LCI Industries (NYSE: LCII), a component supplier to the recreational vehicle and adjacent industries.

Generally, our performance was satisfactory as we were close to our benchmark despite holding nearly 20% of the portfolio in cash. Our smaller capitalization and value orientation were also headwinds. For the year, large cap trounced small, with the S&P 500 returning +21.8%, materially ahead of the Russell 2000's +14.6% return. Growth also trumped value, with the Russell 1000 growth index (RLG) returning +27.6%, over twice the +13.6% return of the Russell 1000 value index (RLV).

In 2017, the S&P 500 outperformed the Russell 2000 by 720bps…

…while growth outperformed value by 1,400bps.

During the year, our two largest capitalization investments, Newell Brands Inc. (NYSE: NWL) and Baker Hughes, a GE Company (NYSE: BHGE) were modest detractors from performance, with negative contribution of -62bps and -29bps, respectively.

We inherited our position in Newell in April, 2016 upon the sale of Jarden Corporation for cash and stock in a transaction valued at nearly $18 billion. We initially invested in Jarden in early 2012 at an equity valuation of less than $3 billion. While we were partially cashed out of our position in the sale, we entered 2017 with a ~1.8% position in Newell. Given the potential for nearly $1 billion in synergies and cost savings from combining the two companies, and Newell's apparently attractive market positions, we decided to retain our position.

Since the closing of the transaction, we have struggled to understand and track a diversified multinational conglomerate of businesses spanning baby goods to kitchenware to glue and pens. Management has evidently also struggled to understand and manage and integrate the businesses, which have also been negatively impacted by destocking in the retail channel and the bankruptcy of Toys'R'Us, a key retail partner in the baby category. Newell management is now facing a Starboard-led proxy contest which seeks to reinstall the former Jarden management team. We have decided that in future, we will generally exit a position following a transaction rather than re-underwriting an investment in the acquiring company, particularly when we have no experience in the acquirer's product markets. Perhaps because we had a better sense of value in the movie exhibition industry we had fully hedged our exposure to AMC Entertainment Holdings, Inc.'s (NYSE: AMC) prior to the closing of the acquisition of portfolio company Carmike Cinemas, Inc. (NASDAQ: CKEC) in late 2016.

We wrote about our investment in Baker Hughes Corporation (NYSE: BHI) in our first quarter 2015 investor letter, in which we described our investment criteria for pursuing potential investments in the beaten-down energy services sector. At the time, we believed that Baker Hughes was one of the market leading services franchises, with the balance sheet and free cash flow characteristics that would ensure its survival through a commodity price downturn of uncertain depth and duration. As with our investment in Newell, we have struggled to understand a company with diverse operations, end market drivers and geographies. As a result, we never grew our position beyond an initial toe-hold of around one percent.

By way of comparison, around the same time, we increased our investment in Natural Gas Services Group, Inc. (NYSE: NGS), a smaller capitalization domestic provider of well head compression services. Since calendar year end 2014, NGS has increased its net cash position from $6.2 million to $72.9 million[2] as it curtailed expansion capital expenditures during the downturn. We enjoy a good relationship with CEO Steve Taylor, a disciplined capital allocator who doubles as investor relations manager. In future, we will stick to our focus on smaller capitalization companies where our research process provides us with differentiated insight; where the narrower scope of activities makes the business easier to understand and where we have an opportunity to develop a meaningful dialogue with management over the course of a multi-year relationship.

Volatility has returned to the stock market. Since achieving a closing high of 2,873 on Friday, January 26, the S&P 500 fell -10% in the nine subsequent trading sessions, thereby ending the record 404 trading day period without a 5% drawdown and the low-volatility regime which had persisted since early 2016. The catalyst for the move was the February Employment Situation report from the Bureau of Labor Statistics, which highlighted a 75 cent or 2.9% year over year increase in average hourly earnings and a 4.1% unemployment rate, perhaps indicating that a tight labor market might be exhibiting inflationary pressure. The yield on 10-year Treasury bonds continued to rise, eventually reaching 2.86%, about 50 basis points above the average yield over the previous 12 months and above the S&P 500's ~2% dividend yield. As market participants pondered these moves, equity market volatility spiked, rising from a closing level of 11.1 on January 26 to 17.3 on Friday, February 2 and 37.3 on Monday, February 6. As volatility erupted, exchange-traded notes (ETNs) designed to profit from declining volatility imploded. The largest such ETN, the XIV, sponsored by Credit Suisse, which had returned over 300% from the start of 2015 through the end of 2017, lost over 90% of its value.

While the ~$5 billion in losses suffered by holders of the short-volatility ETNs must have been painful, they cannot fully explain the market rout. The VIX was first introduced in 1993 and measures the implied volatility of options written on the S&P 500 index. It was quickly dubbed Wall Street's "fear index", rising during periods of market stress (by way of comparison to the current period, the VIX reached 44 in March, 2009) and falling during periods of market calm. Volatility, because it could be precisely calculated, became a key input into risk and portfolio management models. Investors including risk-parity funds (which use leverage such that each

[2] As of September 30, 2017.

asset class contributes equal amounts of "risk" to the portfolio); insurance company variable annuities (particularly managed volatility funds) and commodity trading advisors (CTAs) all use volatility to calibrate equity exposure. The so-called "vol-targeting" industry may have nearly $1 trillion under management in such strategies. A period of subdued volatility will lead the algorithms to increase equity exposure. As volatility spiked, the opposite occurred, with estimates of $80-100 billion in sales from such funds. As volatility itself became a tradeable asset, its value was driven more by money flows which distorted its signaling value. Said another way, subdued volatility was the result of substantial bets on a continued decline in volatility, not a reflection of a risk-less market environment.

While the recent uptick in volatility may be due to the unwinding of this technical feedback loop, markets are also grappling with the implications of a regime change from the era of negative real interest rates, quantitative easing and easy financial conditions, to one characterized by rising real interest rates, higher inflationary expectations and tighter financial conditions. Higher discount rates reduce the present value of future cash flows and will pressure multiples. Growth in earnings, rather than multiples, will have to drive the market from here. Stronger economic growth is a double-edged sword for investors as growth may pressure margins as a result of higher labor and commodity costs. Equities are also discounting continued modest economic growth and no recession. We continue to underwrite our portfolio using conservative assumptions and stress scenarios, including a modest recession within our forecast horizon, so that we can assess the impact of a near term earnings decline on valuation and on balance sheet metrics. We retain a material cash allocation of about 18% to maintain sufficient dry powder to take advantage of opportunities as they arise. After all, we have learned that opportunities to make bargain purchases usually occur during periods of market stress.

During the year, we achieved our ten year anniversary. Since starting the fund, we have become better security analysts and have dramatically improved our portfolio management capabilities. We have been fortunate to work with many highly capable and effective management teams. It has been a privilege to have been entrusted with the management of your capital. We completed our move to Mill Valley in Marin County, just north of the Golden Gate Bridge, shortly before year end. We invite you to come and visit any time. We are looking to grow our team of research analysts. Please send hard-working, thoughtful and capable candidates in our direction. Please note that we anticipate finalizing the 2017 audit this week and distributing the audited financial statements and investor Schedule K-1s in early March. As ever, we are grateful for your interest and support.

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An investment in the Fund is speculative and involves a high degree of risk, including loss of principal, and is suitable only for sophisticated and qualified investors. Please see the Offering Documents for full details regarding the investment strategy, risk factors, liquidity terms, fees, expenses, conflicts of interest and minimum investment amounts.

Performance since inception calculations are based on an investment made in the Fund at inception on July 1, 2007. Fund performance is shown net of all fees and expenses and is unaudited. Returns may vary by limited partner depending on date of investment, high water mark if applicable, participation in new issues and differing management and incentive fees. Past performance is no guarantee of future results and there can be no assurance that the Fund will achieve comparable results in the future.

The Russell 2000 and S&P 500 are not directly comparable to the Fund's performance. The presentation of their returns does not reflect a belief by Spitfire Capital LLC that the Fund is an investment alternative to either index or is comparable to them in any way. The data is included only to provide an indication of the general performance of US equity markets during the periods for which the Fund's performance is presented. Index returns assume reinvestment of dividends.

Any reference to "margin of safety" does not imply that investments made by the Fund are safe. "Margin of safety" is an investment term that refers to the difference between the intrinsic value of a security and its market price.

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