Kinetics Mutual Funds
First Quarter 2017 Commentaries

The Paradigm Fund

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Dear Fellow Shareholders,

The beginning of 2017 has offered little relief to the long maligned value investment community; worse yet to active value investors. This can be quantified, by imperfect proxy, through the relative underperformance year-to-date of the iShares S&P 500 Value ETF ("S&P 500 Value") compared to the broader S&P 500 Index ("S&P 500") or (worse yet) to the iShares S&P 500 Growth ETF ("S&P 500 Growth"). The broader index outperformed the Value index by nearly 300 basis points, while the Growth index outperformed by over 500 basis points. Of course, this is of no concern to the ETF provider because the ETF performed precisely in line with its benchmark (the S&P 500 Value Index). One cannot chastise an ETF for tracking the asset class that it is intended to track.

Active managers of all styles, ranging from value to growth, struggled similarly this quarter. The barometer for active managers is almost ubiquitously the broad S&P 500; as a result, comparisons to the S&P 500 Value Index, while more favorable for value managers, are seldom of interest to disappointed clients. The expectation is that active managers should outperform everything, all of the time—in contrast, ETFs simply track sections of the market. So it is.

Perhaps the larger challenge has been the lack of market breadth this year. Breadth is a very general term associated with directional market factors as they apply to market constituents. For instance, technical traders may refer to the percentage of companies trading above a certain moving average level. We prefer fundamental driven metrics, such as the performance leadership of the index. This was an often cited statistic during 2015 when the notorious "FANG" stocks (Facebook, Amazon, Netflix and Google) dominated market returns. There is a return to this dynamic this year, although we can now include Apple and Microsoft in the calculation, which happen to be the two largest weights in the S&P 500. Collectively, Apple, Microsoft, Amazon, Facebook and Alphabet (Google via two share classes) represent approximately 12% of the S&P 500. These companies have returned an average of 21.59% this year (ranging from Microsoft up over 30% to Alphabet up over 7%), contributing approximately 270 basis points, or nearly half of the S&P 500's return. Investors that are expected to outperform the broad market have little hope of achieving this result unless they own, or even overweight, these companies in their portfolios.

We adhere to strict value investing principles because we believe that this strategy will outperform the broader market significantly in the fullness of time, and when one looks at our long-term record, the Fund has done so, by a considerable margin. There are a few related factors that we believe contributed to these long-term returns, most notably purchase price discipline. This mitigates permanent losses, enables compounding of capital, as well as providing higher upside potential.

Though it may seem simplistic, the key part of the analysis is focused on the price being paid for the asset, which, when considered in conjunction with a qualitative assessment of the business, results in a reasonable framework for investing. Deviations from purchase price primacy tend to skew further toward forecasts of future developments, adding conjecture to the investment. We prefer to root our investments in known quantities.

But there is a larger problem yet for active value investors: what to do when there are few large stocks that meet value investing criteria? There is an institutional impetus to be fully invested at all times, regardless of the opportunity set. The logic might be that active managers should be able to position "defensively" in such circumstances. In any event, the previously mentioned laggard iShares S&P 500 Value Index ETF is currently sporting a price-to-earnings ratio of over 18x and price-to-book ratio of over 2x, after appreciating nearly 20% over the past year. Let's place these valuation metrics into context, examining the top 10 holdings of the index:

Company	Position weight (%)
EXXON MOBIL CORP	3.66
BERKSHIRE HATHAWAY INC CLASS B	3.40
JPMORGAN CHASE & CO	3.37
AT&T INC	2.74
WELLS FARGO	2.70
BANK OF AMERICA CORP	2.54
CHEVRON CORP	2.19
CISCO SYSTEMS INC	1.82
CITIGROUP INC	1.78
GENERAL ELECTRIC	1.48

Source: iShares as of 3/31/2017

The top holdings include two major integrated energy companies and four major diversified banks. The energy companies hold interests in diverse businesses across the world, but are focused on upstream exploration and production activities. These companies have amassed enormous portfolios of operating assets in projects that were profitable at oil prices over $100; the economics are far less appealing at the current prevailing price of approximately $50. These companies are, in fact, directly impaired by the great advances in modern drilling techniques, driving increased unconventional domestic oil and gas production. These companies did not enter these types of resources until far later in the development curve, paying significant prices to do so. In order maintain shareholder loyalty, and stock prices, the companies have been raising dividends, to the point where debt has risen considerably and dividend coverage exceeds free cash flow.

The four major banking institutions are similarly diversified across many lines of businesses, but the basis of the earnings is driven by balance- sheet- based activities, i.e., lending. These companies benefit from higher interest rates to the extent that higher short-term rates drive a steeper yield curve (or higher long-term rates), creating a spread. Despite the measures of the Federal Reserve, the U.S. 10-Year Treasury yield ended the quarter slightly lower than at year end, but the 2-Year

Treasury yield was slightly higher, resulting in a flattened yield curve or lower spread. Also consider that under new regulations, these banks typically leverage assets approximately 10x. A successful return on assets might be 1% for the banks, thus translating into a 10% return on equity using 10x leverage.

Valuation multiples are objective measures, but their interpretation and application is highly subjective. In order to bridge this gap, we have tried to provide context for what an investor is receiving for the current multiples they are paying. All else equal, we interpret such investments as offering very low long-term rates of return (or worse). Time will tell. In the interim, we will avoid such companies and remain dedicated to finding value opportunities that meet our strict criteria. As has been the case in recent history, these companies are increasingly found outside of index/ETF pools.

Paradigm Fund **Top 10 Holdings (%) as of March 31, 2017**	
Texas Pacific Land Trust	21.0%
The Howard Hughes Corporation	10.4%
Icahn Enterprises LP	4.7%
Brookfield Asset Management Inc. - Class A	4.1%
Liberty SiriusXM Group - Class C	3.1%
Live Nation Entertainment, Inc.	2.7%
Onex Corporation	2.4%
Liberty Broadband Corporation - Series C	2.3%
EchoStar Corporation - Class A	2.2%
The Wendy's Company	2.1%

Important Disclosures

You should consider the investment objectives, risks, charges and expenses of the Fund carefully before investing. For a free copy of the most recent Prospectus, which contains this and other information, visit our website at www.kineticsfunds.com or call 1-800-930-3828. You should read the Prospectus carefully before you invest. Performance data quoted represents past performance, which does not guarantee future results. Investment return and principal value of an investment may fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit www.kineticsfunds.com for the most recent month-end performance data.

Portfolio holdings information, if any, is subject to change at any time and is as of the date shown.

The opinions expressed are not intended to be a forecast of future events, or a guarantee of future results, or investment advice. Additionally, the views expressed herein may change at any time subsequent to the date of issue hereof.

The Paradigm Fund is classified as a non-diversified fund. Therefore, the value of its shares may fluctuate more than shares invested in a broader range of industries. In a non-diversified fund, more of the Fund’s assets may be concentrated in the common stock of any single issuer, which may make the value of the Fund's shares more susceptible to certain risks than shares of a diversified mutual fund.

In addition, investing in foreign securities involves more risk than just U.S. investments, including the risk of currency fluctuations, political and economic instability and differences in financial reporting standards. There may also be heightened risks investing in non-investment grade debt securities and the use of options. There are also risks associated with investing in small and medium sized companies. Non-investment grade debt securities, i.e., junk bonds, are subject to greater credit risk, price volatility and risk of loss than investment grade securities. Options contain special risks including the imperfect correlation between the value of the option and the value of the underlying asset. Please refer to the Fund's prospectus for a complete list of risks and fees.

The S&P 500® Index represents an unmanaged, broad-based basket of stocks. It is typically used as a proxy for overall market performance. Index returns assume that dividends are reinvested and do not include the effect of management fees or expenses. You cannot invest directly in an index.

Unlike other investment companies that directly acquire and manage their own portfolios of securities, the Paradigm Fund pursues its investment objectives by investing all of its investable assets in a corresponding portfolio series of Kinetics Portfolios Trust.

You will be charged a redemption fee of 2.0% of the net amount of the redemption if you redeem or exchange your shares 30 days or less after you purchase them.

Distributor: Kinetics Funds Distributor LLC is an affiliate of Kinetics Asset Management LLC, and is not an affiliate of Kinetics Mutual Funds, Inc.