Kinetics Mutual Funds
First Quarter 2018 Commentaries

The Market Opportunities Fund

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Dear Fellow Shareholders,

Capital markets are simply a mechanism for businesses and entrepreneurs to source capital which can be deployed at higher rates of return. Providers of capital seek to earn adequate returns on their investments, presumably commensurate with the risk of the endeavor. This is most simple with debt funding, as the lender provides capital at a certain interest rate over a predetermined period of time. The recipient of the capital seeks to earn a higher rate of return and repay the principal upon maturity. Equity valuation is a much less objective exercise, as the return is generally driven primarily by capital appreciation, less so by interest. Also, the cost of equity funding is highly subjective – academics' and bankers' standardized cost of equity metrics use inputs that make no distinction between equity valuations.

Increasingly, it has become very difficult to source equity investments that we believe provide adequate return potential. High equity valuations imply ambitious expectations for future growth, theoretically justifying the high multiples. Often, this growth is highly subjective, as are future profit margins and returns on invested capital. Thus, we find this type of investing to be inordinately high risk, despite attractive returns recently.

Historically, equity investors could earn reasonable rates of return in fixed income securities during periods of equity market exuberance. However, due to a confluence of factors, many of which are not market forces, investment grade and U.S. government bonds scarcely cover the cost of inflation. Thus, we choose to adapt to the current environment by increasing our concentration in our equity portfolio, while also increasing cash balances. This seeks to isolate equity return alpha, minimizing market correlations, while cash balances offer the ability to reallocate capital at superior risk-adjusted terms in the future.

Concentrated equity portfolios are anathema to modern portfolio theorists, who consider this concentration to be equivalent to higher risk. However, we believe that a concentrated portfolio of idiosyncratic companies that offer superior risk and return profiles to the broader market actually reduces risk, particularly during periods of broader market excesses.

The largest position in the portfolio is truly unique, and in this case, the financials are beginning to elucidate that of which we have long been aware of. The company earns over a 90% operating margin and greater than a 70% net margin. Sales in the first quarter have grown nearly 150% compared to the prior year, while net income has nearly tripled (assisted by the federal tax rate reduction). Furthermore, the company holds a net cash balance equal to 5x cumulative operating expenses over the trailing year. Annualizing first quarter earnings, which may prove to be overly conservative, the forward earnings multiple is approximately 27x.

While 27x earnings is certainly not a value in isolation, we believe we have great clarity into quantifiable earnings growth over the next 5+ years that is vastly in excess of the broader market and GDP. Quantifiable growth is rare in any business, let alone the broader market. However in this case, the company owns the land and mineral rights associated with a multi-billion dollar buildout of the Delaware Basin, directly associated with the activity of one of the largest oil and gas companies in the world. This is a very different growth dynamic compared to market share and margin growth assumptions for global internet shopping, cloud infrastructure and digital advertisements.

Finally, it should also be noted that the company recently began capital expenditures related to a water resource business amounting to approximately $18 million in 2017. We believe that a minor portion of this expenditure figure has driven an $8 million incremental gain in water related revenue compared to the 4th quarter of last year. As the fixed assets from trailing capital expenditures are delivered and placed in use, we believe that we will experience similar returns on invested capital. This is an enterprise that we are eager to fund.

Concentrated equity portfolios require extensive understanding of individual businesses, along with the conviction to invest accordingly. High cash balances are paradoxical to most institutional money managers, as the view is to always find opportunity in equities. The mathematics of compounding are far more attractive if cash softens the inevitable market declines over time. We view equity investing as akin to investing in individual businesses – much like we would never desire to invest in all of the businesses in the country, at all times, we choose to be very selective and disciplined with public equity investing.

Market Opportunities Fund **Top 10 Holdings (%) as of March 31, 2017**	
Texas Pacific Land Trust	23.5%
The Bitcoin Investment Trust	7.9%
Icahn Enterprises LP	2.9%
The Howard Hughes Corporation	2.7%
Dream Unlimited Corp. - Class A	2.5%
Onex Corporation	2.1%
Associated Capital Group, Inc. - Class A	1.6%
Partners Value Investments LP	1.6%
Visa, Inc. - Class A	1.2%
CME Group, Inc.	1.2%

Important Risk 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.

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.

The Fund holds investments that provide exposure to bitcoin. The value of bitcoins is determined by the supply of and demand for bitcoins in the global market for the trading of bitcoins, which consists of transactions on electronic bitcoin exchanges ("Bitcoin Exchanges"). Pricing on Bitcoin Exchanges and other venues can be volatile and can adversely affect the value of the bitcoin. Currently, there is relatively small use of bitcoins in the retail and commercial marketplace in comparison to the relatively large use of bitcoins by speculators, thus contributing to price volatility that could adversely affect a portfolio's direct or indirect investments in bitcoin. Bitcoin transactions are irrevocable, and stolen or incorrectly transferred bitcoins may be irretrievable. As a result, any incorrectly executed bitcoin transactions could adversely affect the value of a portfolio's direct or indirect investment in bitcoin. Only investors who can appreciate the risks associated with an investment should invest in cryptocurrencies or products that offer cryptocurrency exposure. As with all investments, investors should consult with their investment, legal and tax professionals before investing, as you may lose money.

As a non-diversified Fund, the value of its shares may fluctuate more than shares invested in a broader range of companies. 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.

Unlike other investment companies that directly acquire and manage their own portfolios of securities, the Fund pursues its investment objective 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.

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.

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