AZARIAS CAPITAL

July 2017

	2Q17	YTD	1 Year	2016	Since Inception* 11/1/2015
Azarias Focused Small Cap Value Composite (Gross of Fess)	**9.7%**	**11.1%**	**36.1%**	**36.4%**	**49.1%**
Azarias Focused Small Cap Value Composite (Net of fees)	**8.4%**	**9.4%**	**32.5%**	**31.9%**	**41.6%**
Russell 2000	2.5%	5.0%	24.6%	21.3%	24.9%
Russell 2000 Value	0.7%	0.5%	24.9%	31.7%	29.0%

**Periods greater than one year are cumulative. See below for important disclosures.*

Dear Friends,

We were pleased with the broad strength exhibited in our Focused Small Cap Value strategy during the second quarter. Despite the strong performance, we believe the portfolio continues to be well positioned going forward. Many of the largest positions have yet to contribute to the portfolio's results. For example, the two portfolio companies with exposure to uranium have not demonstrated fundamental improvement or stock price appreciation. We provide an update on our uranium thesis below.

In terms of sector exposure, the strategy maintains sizeable overweights vs. the Russell 2000 in Industrials (+5.6%), Materials (+10.3%) and Energy (+10.9%). Notably, the energy sector exposure is entirely due to the uranium positions.

Financials represent the major sector underweight in the portfolio with a 0% weight vs. 18.1% in the Russell 2000. As we stated in our 1Q17 letter, financials are not a permanent underweight, but we simply have not uncovered any financials that offer the upside in earnings and stock price we require for purchase. However, as we write this letter we are studying an insurance company that may be an attractive addition to the portfolio.

It should be noted that the sector exposure is driven by our bottom up, company specific research as opposed to a top down viewpoint.

Investment Thesis Update – Uranium

All of our decisions are made on a company-by-company, bottom up, fundamental basis. Prior to being added to the portfolio, new positions are evaluated to ensure they possess the four traits necessary for ownership, a research process we have dubbed **"The 4 Cs": 1) Change; 2) Cheap; 3) Competitively Stable; and 4) Conservatively Financed.** However, we often find more than one company in a commodity industry that meets our criteria. In that case, the companies share a common "Change" thesis, and that is an expected recovery in the underlying industry.

Our investments in two uranium companies constitute our largest holdings and our largest sector overweight versus the index. We think the investment prospects for these two companies remain very compelling. They are excellent examples of how we exploit industry cyclical recoveries (aka change) to generate returns.

We originally became interested in uranium in 2014 when the spot price of the commodity dropped to $28 per pound from a 2011 peak of $72 per pound and the all-time high above $150 per pound set in 2007.

Our research suggests roughly 25% of global uranium production loses money on an "all-in" cost basis at prices below $40 per pound compared to the current spot price of about $20 per pound. Because the spot price of uranium has been below $40 per pound for most of the past four years, producers have rationally curtailed production at existing, high cost mines and cancelled capital-intense expansion projects. As a result, new supply growth of uranium will be very low over the next several years. We would not expect the industry to consider expansion projects until the price of uranium exceeds $65 per pound, the price required to economically justify incremental investment in capacity.

However, there are 59 nuclear reactors currently under construction globally, primarily in India and China. This will cause demand for uranium to increase roughly 30M pounds (+15%) by 2021, net of closures in the U.S. and Europe. This increased uranium demand combined with low supply growth will result in a supply deficit by 2021 according to our estimates. However, it takes several years to refine raw yellowcake into enriched uranium, requiring nuclear power plants to procure uranium two to three years in advance of their needs. Therefore, the coming supply deficit in uranium should begin to be reflected in higher uranium prices in the next 12-24 months.

The uranium equities that we hold are low cost producers with attractive long-term contracts to supply uranium at economic prices, i.e. they are <u>competitively stable</u>. This has enabled them to generate positive cash flow even at the low point in the cycle, suggesting each has <u>conservatively financed</u> its balance sheet. Both are well positioned to thrive as industry fundamentals recover, and we believe each stock is trading 50% or more below fair value, i.e. they are <u>cheap</u>. Together, they represent nearly 15% of the portfolio. Notably, we believe demand for uranium is relatively immune from the overall economic cycle, making these stocks good diversifiers as well as attractive on their own merits.

Areas of Interest

We have several new ideas currently under evaluation. We think there may be an opportunity in the North American oil and gas sector. We know the world needs oil production from the United States to meet global demand, and we believe the recent sell-off might have caused some oil field service companies to become undervalued. Additionally, we are investigating an insurance niche where recent underwriting results have been unprofitable. We expect underwriters to respond by raising prices and getting profitability back to an acceptable level.

At the Firm

Our research team is focused on finding new ideas to keep the portfolio fresh and monitoring existing positions. With the January addition of Rob Lodge, we began to extend our reach in terms of new business development, and a healthy pipeline of opportunities has been established and is growing. Assets under management at the firm have nearly doubled since the end of 2016, and we remain optimistic on the portfolio as well as the business.

AZARIAS CAPITAL

Thank you for your interest in Azarias. If you have any questions, please call or email Rob Lodge (215-494-3360) or me directly.

Best Regards,

Daren Heitman

Azarias Capital Management L.P. is registered as an investment adviser with the Pennsylvania Department of Banking and Securities. Registration with the SEC or any state securities authority does not imply a certain level of skill or training.

PERFORMANCE RETURNS
The Focused Small Cap Value Composite (the "Composite") represents the returns of all discretionary, fee-paying portfolios with a concentrated U.S. equity small cap value investment mandate. New portfolios are included in the Composite at the start of the next month following full investment of the accounts assets; terminated portfolios are included in the Composite up to the last full measurement period (last full month) that Azarias retains investment discretion. G ross-of-fees returns are presented before management and any performance-based fee, but after all trading expenses. Net-of-fees returns are presented after management fees, any accrued performance-based fee and all trading expenses. Fees vary between accounts in the composite. Composite returns are calculated by asset-weighting the individual portfolio returns using the beginning of period portfolio value.

Since inception, the composite includes one portfolio whose net of fee returns are calculated using a management fee rate of 1.5% (highest fee charged to the portfolio) and a performance-based fee of 20% of profits in excess of the Russell 2000 Index. These fees are accounted for on an accrual basis. The gross and net returns of this portfolio include trading and organizational expenses. Actual fees charged to some clients are lower than the standard fee schedule. The firm's standard fee schedule is provided on page 16 of this presentation.

Weightings, exposure, attribution and portfolio characteristics presented reflect estimates of the representative account at the end of the specified period and are the result of classifications and assumptions made in the sole judgment of the adviser. This information is as of the date(s) indicated, may not be complete and is subject to change.

Returns greater than one year are not annualized. The performance data quoted represents past performance. Past performance is no guarantee of future results. Current performance may be higher or lower than quoted. Composite returns include cash and cash equivalents and the reinvestment of any dividend or interest income.

USE OF INDEX
The Russell 2000® Index is a small-cap stock index of the bottom 2000 in the Russell 3000 Index stocks based on market-capitalization. The Russell 2000 Index is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set. The returns of the index include the investment of dividends but do not account for transaction costs and operating expenses, which an investor might incur in attempting to obtain such returns. If an index had expenses, its performance would be lower. You cannot invest directly in this index.

The Russell 2000® Value Index is a subset of the Russell 2000 Index and measures the performance of the stocks with lower price-to-book ratios and lower relative forecasted growth rates. The returns of the index include the investment of dividends but do not account for transaction costs and operating expenses, which an investor might incur in attempting to obtain such returns. If an index had expenses, its performance would be lower. You cannot invest directly in this index.

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