TARKIO FUND

A No-Load Mutual Fund Managed by:
Front Street Capital Management, Inc.

In this quarter's Tarkio Fund (the "Fund") shareholder letter, I'd like to explore a question that is always in the back of our minds when we make investment decisions: "When push comes to shove, how powerful is our investment criteria?" A question that makes The Container Store the perfect subject for this letter.
As always, let's take a quick look at the criteria we at Front Street Capital (the Fund's investment advisor) use for selecting companies for long-term ownership in the Fund. We generally look for companies that feature:

- Integrity of Management
- Long-Term Focus
- Purpose and Passion
- Employee Empowerment – Driving Fear Out of the Organization
- Teamwork – Cooperation, Not Competition
- Disciplined Capital Allocation

Are these qualities powerful enough to carry a company when the chips are stacked against it? We think the story of The Container Store provides us with a good indication that this is the case.

Our relationship with The Container Store really started out as a story about Whole Foods Market. As many of the Fund's long-term shareholders know, Whole Foods was a core position from the Fund's inception until the company's acquisition by Amazon in 2017. John Mackey, the founder of Whole Foods, developed a corporate culture for his company that we believed was as consistent with our investment criteria as we had ever seen. Mackey felt the progressive culture that was created at Whole Foods was not just important for his company, but that it could be used as a template for enlightening business leaders across the globe. He felt that the best way to maximize long-term value for a company's shareholders was to serve a greater purpose for society, and to engage every employee in the company along the way. In 2012 he collected his ideas and experiences in the bestselling book *Conscious Capitalism*. Even before that, John and his college roommate Kip Tindall, and a group of other likeminded thought leaders launched the Conscious Capitalism movement, which is still active today. As you may have guessed, Kip Tindall was the founder and longtime CEO of The Container Store.

The Container Store is a retailer with traditional brick and mortar roots. It specializes in helping its customers better organize their lives. In other words, The Container Store sells a lot of empty boxes. But it does so with passion and purpose. Tindall refers constantly to a set of seven "foundation principles" that put employees, customers and vendors first. The company is known for its vendor relationships as well as its engaged team members. As a result, The Container Store has one of the lowest employee turnover ratios in retail, almost ten times lower than the industry average[1]. And it has developed a multitude of dedicated and loyal customers! Check out The Container Store's website to get a better sense of the company's "yummy" culture.

Despite tremendous early success, The Container Store stayed a private company for a surprisingly long time given its enviable track record. Finally, the company launched an initial public offering in 2013 at $18.00 per share. The long-anticipated IPO was favorably embraced by the investment community, and within months the stock had risen to over $43.00 per share. Although we normally have little interest in investing Fund assets in IPOs, we took a long look at The Container Store due to its superb culture. In the end, even though the culture aligned with our criteria, we felt the valuation wasn't appealing. One of the big benefits of taking a growing company public is to raise cash to accelerate growth initiatives. However, we thought the structure of the Container Store IPO wasn't ideal. The company went public with over $300 million in debt and minimal cash reserves, which we felt was not ideal for a company with only $600 million in sales. We decided not to buy at that time.

---

[1] "Our Employee First Culture." What We Stand For: Organization with Heart. 2010. Accessed August 07, 2018. http://standfor.containerstore.com/putting-our-employees-first/.

218 E. Front St. Suite 205, Missoula, MT 59802 406-541-0130 www.frontstreetcap.com www.tarkiofund.com

Not too long after The Container Store's IPO, investors across the retail sector began to recognize and fear the "Amazon effect" as same store sales numbers across the entire retail sector began to falter. The Container Store's stock was hit particularly hard. When the stock had fallen to $8.00 per share, we bought a token-sized position in the Fund, although we were still concerned about its elevated debt levels.

As we know, manic Mr. Market can turn an industry transition into full-blown hysteria. Suddenly, instead of recognizing that retail companies were trying to strike a balance between online and in-store sales, Wall Street seemed to decide that physical retail sales would go the way of the brontosaurus. Retail stocks came under siege for a solid two-year period.

While it seemed that investors were generally panicking, we tried to remain clear-headed in the retail downturn. For example, it was an easy decision for us to begin reaccumulating Costco (a retailer that is one of our all-time favorite cultural rock stars) at attractive prices in the Fund. But The Container Store seemed to be a different story. It looked like a perfect cultural fit for us, but the company remained saddled with debt and was squarely in the crosshairs of the "Amazon effect". After all, it is a brick and mortar retailer that sells empty boxes! We started (internally) to refer to the company as "The Lowly Container Store," a tongue-in-cheek acknowledgement of Wall Street's disdain for brick and mortar retail and, in particular, The Container Store.

We were faced then with our thesis question: How powerful was our criteria? Could it power a company through an industry storm without other competitive advantages and a less than ideal balance sheet? Finally, the stock fell under $4.80 per share and we started to accumulate a bit more in the Fund. When it fell under $4.00 – ultimately reaching $3.57 per share (with approximately $18.00 per share in sales and $6.00 per share book value) – we started buying in earnest, bringing the position to over 3% of the Fund.

As has been our experience for over thirty years in investing, culture wins in the end. The Container Store, buoyed by its fantastic culture and employee environment, eventually stabilized. This past quarter saw same store sales up 3.5 percent and cash flow increased to the point where the company has been able to begin paying down meaningful amounts of debt. At the time of writing, the stock is selling around $12.02 per share.

If there was any doubt in our minds (there wasn't) that our criteria are a powerful competitive advantage in selecting companies that can outperform their peers over the long-term, there is certainly none now. Our experience with "The Lowly Container Store" has reignited our enthusiasm for our criteria, our beloved long-term companies, and our ability to continue what we believe to be strong long-term performance. After all, while all else changes, human nature stays the same.

We thank you for your long-term investment in the Tarkio Fund, and we will never take your continued confidence for granted.

Warm regards,

Russ Piazza

Russ, Michele, Ginger, Jeremy, and Dominic
The Tarkio Team

On September, 2018, The Container Store (TCS) was 5.11% of the Tarkio Fund Portfolio at a share price of $11.10 per share. The mention of any investments in this commentary should not be considered a recommendation to sell or purchase the security(ies) mentioned or similar investments. Please consult an investment professional on how the purchase or sale of such investments can be implemented to meet your particular investment objective or goals. Investments in securities and/or similar investments are subject to risks. It is important to obtain information about and understand these risks prior to investing.

Mutual Fund investing involves risk. Such risks associated with the Tarkio Fund (including but not limited to Small/Medium Capitalization Risks, Foreign Securities Risk, Fixed Income Securities Risk, Non-Diversification Risk, and New Fund/Adviser Risk) as well as applicable investment objectives, charges and expenses must be considered carefully before investing. This and other important information about the Tarkio Fund is found in the Prospectus, a copy of which or current performance information may be obtained by visiting www.tarkiofund.com or by contacting 866-738-3629. We encourage you to read the prospectus before investing.

Tarkio Fund is distributed by Arbor Court Capital, LLC - Member FINRA.