



Dear Partners & Friends,

For the third quarter 2023, Ace River Capital Partners, L.P. (the “Fund”) returned -22.85%. Over the same period, the S&P 500 (SPX) and Russel 2000 (RTY) Indexes returned -3.3% and -5.1%, respectively.

Strategy

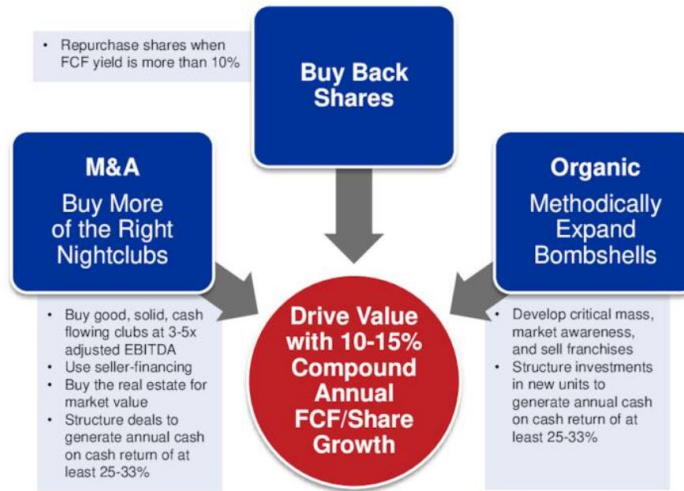
My goal is to maintain a concentrated portfolio of small and micro-cap companies with unique advantages and growth potential within their respective industries. The aim is to hold them for the long term. Finding such companies requires significant time and effort. Due to the scarcity of suitable opportunities, constraints on time and resources, and opportunity costs, I will take substantial positions in the companies that meet my criteria and pass my risk/reward assessment. I do not subscribe to wide diversification and only research and follow a limited number of companies deeply. I will not spend much time on a company if I am unwilling to take a substantial position and have the conviction to add to that position on weakness. This approach requires a lot of research and patience. There will be long periods of inactivity with few trades, and I will rarely hold more than 5 companies at a time. I will normally aim to have one short position. The short position will usually target a much larger company than the small and micro-cap companies held as long positions. This strategy accepts short-term volatility in pursuit of higher, long-term, tax-efficient returns.

Top Position

The fund’s top position is RCI Hospitality (RICK). RICK is the only publicly traded owner of adult nightclubs in the US. Currently they own 56 clubs across 13 states and an additional 13 sports-bar restaurants with the “Bombshells” concept that has recently begun franchising. With few municipalities issuing new adult entertainment licenses these businesses function as local monopolies with excellent unit economics. The Bombshells segment works well as an alternative investment if no attractive acquisitions are available, and the share price is trading higher than the repurchase target range. (See Capital Allocation Strategy below).

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Capital Allocation Strategy*



* We may deviate from this strategy if other strategic rationale warrants

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The stock has seen a large drawdown of 40% from its highs in the 90s earlier this year. The company has estimated its FCF for FY24 to be in the \$68M-\$78M range and provided the slide below in its Q2 earnings presentation.

FCF Stock Yield

Key Metric

- After-tax yield on Free Cash Flow (FCF) relative to our market cap

Buy Back Shares If FCF Yield...

- Exceeds double-digit range or exceeds yield of accelerated payment on our highest interest debt

Current Status

- Assumptions
 - FY24 range of \$68M-\$78M
 - 9.43M shares
- ~\$72-83 per share is the point between buying/opening units and buying shares

FCF Yield on Stock Price @ FY24 Range of \$68M-\$78M



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With the stock trading at \$52 at the time of writing, it is well under the lowest presented buyback target price in the range of \$72-83. This represents greater than a 10% conservative cashflow yield since the company targets a min 10% FCF yield for repurchases, and the stock is substantially under this target. The market seems to have reacted negatively to the recent same-store sales comparisons and economic outlook. The same-store sales comparisons are negative when compared to the post Covid bounce period. With all segments profitable and a clear capital allocation strategy, RICK continues to be my top pick for the next 5-10 years.

Second Largest Position

Drive Shack (DSHK) is a unique and innovative leisure and entertainment company that offers guests an immersive experience through its state-of-the-art driving ranges, golf courses, and now, its latest offering – The Puttery mini-golf venues. The company has gone through major disruption and changes in the last year, with its delisting and the appointment of a new CEO and CFO. The last quarter it was able to report its first profit as predicted with the addition of a couple recent Puttery venues. I will be watching closely as the next few quarters should either serve as a foundation for lift off or present the pitfalls to bankruptcy. I believe the upside is extremely high from this point and the likelihood of the company stabilizing presents a great asymmetric risk/reward opportunity moving forward.

Third Position

MarineMax (HZO) operates a vertically integrated boat and yacht company with manufacturing, retail sales, financing, insurance, all the way down to maintenance and storage operations. The company has a strong portfolio of marinas and is in a great position to be able to roll up additional retailers, marinas, and storage facilities. I do wish the company would provide more information on its capital allocation strategy and how it thinks about the decisions to target retailers, real estate/marinas, or share repurchases. This would provide foresight for investors and keep management accountable for decisions. RCI Hospitality has a capital allocation strategy slide mentioned earlier in this letter, that is the type of thing I would love to see from MarineMax. I will attempt to bring this up to management. Until I can gather more information about the capital allocation strategy this will remain my lowest conviction holding but trading at just 3x cash with a strong position in the high margin/high cost segments of the boating industry I like the entry point.

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Thank you for reading. Please reach out for any reason.

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