Q2 | 2021

SMID Cap

THE LONDON COMPANY

Market Observations & Portfolio Commentary

Quarterly Market Update

US stocks posted mid to high single digit gains during Q2. Solid economic data and improving corporate earnings were positives, partially offset by concerns about rising inflation, the timing of potential changes to monetary policy from the Fed, and the possibility of future tax increases. Growth outperformed Value across the market cap spectrum except in the Small Cap space. For the most part, cyclical sectors outperformed defensive, though it was mixed among mid and Large Cap stocks. With regard to factors driving performance during Q2, the dynamics weren't linear down the market cap spectrum. Amid Large Cap stocks, Growth and Quality factors had the most positive impact on relative performance, while Value factors had a negative impact. Amid Mid and Small Cap stocks, Volatility and Yield had the most positive impact, while the remaining factors produced mixed results.

Key Performance Takeaways for the Quarter

- The London Company Small-Mid Cap portfolio returned 3.4% gross (3.2% net) during the quarter vs. a 5.0% increase in the Russell 2500 Value Index. Both sector exposure and stock selection were headwinds to relative performance.
- We are bottom-up stock pickers, but sector exposures influenced relative performance as follows:
  - *What Helped*: Underweight Utilities & Financials (two weaker performing sectors)
  - *What Hurt*: Underweight Energy (the best performing sector) & overweight Cons. Staples (a weaker performing sector)
- The SMID portfolio trailed the benchmark in Q2, which isn't surprising given the continued low quality, high beta leadership environment amid Mid & Small Cap stocks. Nearly all of the recent performance shortfall during this recovery can be attributed to what we don't own versus what we do. The recent strength of some of the more speculative Small Cap names is not driven by fundamentals nor is it sustainable longer-term.

Top 3 Contributors to Relative Performance

- **Armstrong World Industries (AWI)** – AWI continued its rally in Q2 reflecting improving market conditions and an increased normalization of business/office space operations. The Architectural Billing Index (ABI) is a leading indicator for AWI's business and hit its highest score in April and May since pre-2008. Lastly, the company saw a quicker than expected recovery in pricing during the quarter.
- **Deckers Outdoor (DECK)** – DECK reported an incredibly strong quarter highlighted by 50% topline growth and 100% EPS growth. The UGG brand is resonating with customers leading to strong sales. The HOKA brand is experiencing massive growth and is well on its way to becoming a $1B brand. The balance sheet is strong and management continues to execute on the long-term strategy.
- **Copart (CPRT)** – CPRT performed well in Q2, reflecting solid momentum and market share gains. Average selling prices remain strong, which helped the top and bottom line. CPRT benefits from structural shifts in the industry such as an increase in vehicle complexity, higher repair costs, and stronger auction involvement (international buyers). CPRT has leading market share in all of its markets and continues to widen its moat, which is especially beneficial as volume returns.

Top 3 Detractors from Relative Performance

- **Churchill Downs (CHDN)** – CHDN pulled back during Q2 after strong performance in 2020. We viewed CHDN's execution through the worst of the pandemic as exceptional, and we continue to be positive on management's capital allocation decisions. In our view, the recent underperformance is noise and not indicative of a change in the long-term fundamentals.
- **Citrix (CTXS)** – CTXS underperformed after reporting quarterly results that disappointed investors. Supply chain shortages were a challenge, plus renewal rates fell short of expectations. CTXS' transition to a subscription model is complete, which should provide more consistency in results going forward. We remain attracted to CTXS' strong positioning in an environment that will likely value more flexible work solutions in the future.
- **NewMarket (NEU) –** NEU underperformed following a weak earnings report driven by rising oil and base oil prices combined with growing concerns over the ramp of hybrid and electric vehicles. NEU's margins tend to suffer in periods of rising base oil prices until they roll over, and NEU can capture the lag in spreads. We remain attracted to NEU's positioning in the consolidated market for fuel additives and lubricants.

Trades During the Quarter

- **Received Cash: Varian Medical Systems (VAR)** – Received cash from Siemens Healthineers following closing of acquisition.
- **Initiated: Black Night (BKI)** – BKI engages in the provision of software, data and analytics solutions to large financial institutions to support loan servicing, loan origination, and other mortgage related items. BKI is the industry leader in mortgage servicing, with ~60% market share on first liens and 19% on second liens. Mortgage servicing is a recurring revenue business as the company is paid based on the stock of mortgages outstanding, not the volume of loan originations. BKI works with all the leading banks, and it is much cheaper for banks to outsource this function. Revenue is largely recurring with annual price escalators, and BKI generates very attractive margins. The shares trade at a discount to other software-as-a-service peers despite a more recurring revenue stream.

Looking Ahead

We maintain a positive view on the US economy and expect strong real GDP growth in 2021. Nearly half of the population has been vaccinated, and most of the economy has re-opened. The US consumer is in great shape and labor markets continue to improve. Separately, the manufacturing and services segments of the economy are firmly in expansionary territory. Fiscal and monetary policy should continue to be accommodative in the near-term. Despite the positives, we recognize that risks remain. Inflation concerns, talk of tax hikes, elevated equity valuations, some fiscal stimulus rolling off, and a more reactive Fed are noteworthy factors looming over markets. While we believe fundamental conditions remain positive, we note a confluence of market concerns could lead to increased volatility and more muted returns for equities in the near term. As we look at the characteristics of our portfolios today, the positioning is the best it's been in a number of years. Returns on capital and balance sheet strength continue to be very healthy. Given the level of quality, it is abnormal to see our portfolios trade at such attractive valuations relative to the respective benchmarks. We believe this will serve us well for both near-term volatility and long-term durability.

Past performance should not be taken as a guarantee of future results.

Q2 | 2021

SMID Cap

THE LONDON COMPANY

Performance

As of June 30, 2021

	QTD	YTD	One Year	Three Years	Five Years	Ten Years	Inception to Date
SMID Cap (Gross)	3.4	12.0	36.7	14.1	13.8	12.7	17.1
SMID Cap (Net)	3.2	11.6	35.6	13.3	13.0	11.9	16.3
Russell 2500 Value	5.0	22.7	63.2	10.6	12.3	10.9	15.3

Inception date: 3/31/2009

Contact information

The London Company
of Virginia, LLC
1800 Bayberry Court, Suite 301
Richmond, VA 23226

T 804.709.1244
F 804.649.9447
info@TLCAdvisory.com
www.TLCAdvisory.com

Disclosure notes

The London Company's performances are size weighted and annualized based on calculations for the period ending June 30, 2021. The characteristics discussed herein relate to a representative account, and not every client's account will have these exact characteristics. As London manages its client portfolios according to each client's specific investment needs and circumstances, London cannot affirm that the characteristics of the account shown are similar to all accounts participating in the strategy. This is due in part to the timing of trades by the Adviser, market conditions, cash availability, and the timing of client deposits and withdrawals. Therefore, prospective clients should not assume that similar performance results to those shown would have been achieved for their accounts had they been invested in the strategy during the period. None of the information contained herein should be construed as an offer to buy or sell securities, or as investment recommendations. An investment in a London Company strategy is subject to risks, including the loss of principal.

Definition of Firm: The London Company of Virginia is a registered investment advisor. Registration does not imply a certain level of skill or training. More information about the advisor, including full descriptions of its investment strategies, fees and objectives, can be found in the firm's Form ADV Part 2, which is available upon request by calling (804) 775-0317 or visiting www.TLCadvisory.com. The London Company claims compliance with the Global Investment Performance Standards (GIPS®). GIPS® is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. Please visit www.TLCadvisory.com or contact us at 804-775-0317 to request a complete list and description of The London Company's composites and/or a presentation that adheres to the (GIPS®) standards.

Composite Creation/ Inception Date: March 31, 2009

Composite Definition: The Small-Mid Cap strategy is an extension of our Small Cap strategy with weighted market capitalization higher than our Small Cap portfolio, and is within the market capitalization ranges of the major domestic small to mid cap indices. Accounts in this product composite are fully discretionary taxable and tax-exempt portfolios with a minimum of $100,000 in assets. The product is measured against the Russell 2500 Index and has a creation and inception date of March 31, 2009. There is no use of leverage, derivatives or short positions. All actual fee-paying discretionary portfolios are included in one or more composites that have been managed for a full calendar quarter with limited restrictions and similar objectives. Composite may include accounts under dual contract.

Benchmark Description: Primary: Russell 2500 Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "smid" cap. Russell 2500 is a subset of the Russell 3000 Index. It includes approximately 2500 of the smallest securities based on a combination of their market cap and current index membership. Secondary: Russell 2500 Value Index measures the performance of the small to mid-cap segment of the U.S equity universe. It includes those Russell 2500 Index companies with lower price-to-book ratios and lower forecasted growth values. Benchmark returns are not covered by the report of independent verifiers. The SMID Cap product is typically compared to the Russell 2500 Index. Any comparison to the Russell 2500 Value is for illustrative purposes only.

Performance and Fees: Gross of fee returns are calculated gross of management and custodian fees and net of transaction costs. Net of fee returns are calculated net of actual management fees and transaction costs and gross of custodian and other fees. Returns may be net of miscellaneous fund expenses. The gross figures do not reflect the deduction of investment advisory fees. For example, an account that earned 15% per year for 10 years would have an accumulated return of 305% before fees and 270% after fees, assuming a 1% fee. Returns are calculated and stated in US dollars. Returns are calculated gross of withholding taxes on foreign dividends and interest. Dividends are reinvested. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

Past performance should not be taken as a guarantee of future results. The report is for informational purposes only. Data, while obtained from sources we believe to be reliable, cannot be guaranteed and all statistics are subject to change. The statements contained herein are solely based upon the opinions of The London Company and the data available at the time of publication of this report, and there is no assurance that any predicted results will actually occur. Information was obtained from third party sources which we believe to be reliable but are not guaranteed as to their accuracy or completeness. This report contains no recommendations to buy or sell any specific securities and should not be considered investment advice of any kind. In making an investment decision individuals should utilize other information sources and the advice of their investment advisor.