Portfolio Commentary

2021 Market Update

US stocks posted another year of double-digit returns and new all-time highs. A strong rebound in the US economy in 2021 and historically strong earnings momentum offset concerns over COVID-19 variants, elevated inflation and pandemic related supply chain disruptions.

On balance, it was a micro-driven year, and the market rewarded profitability across sectors, size and styles. Large Cap stocks led Smaller Caps. Stylistically, Growth outperformed Value in the Large Cap space, while Value significantly led Growth among Small and Mid Caps. Defensive shares outperformed the more cyclical shares, but the difference in returns was more evident in the Small Cap space. With regard to factors driving performance, most categories had a positive influence on returns, but the results were mixed within Growth, Volatility, and Momentum factors.

Key Performance Takeaways

The London Company Small-Mid Cap portfolio returned 20.7% gross (19.8% net) for the year vs. a 27.8% 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 & Healthcare (the two weakest performing sectors)
- What Hurt: Underweight Energy (the best performing sector) & overweight Information Technology (a weaker performing sector)

The Small-Mid portfolio gained ground late in 2021, but couldn't make up for the shortfall early in the year when the market rewarded higher beta, more value oriented stocks. Traditional Value sectors like Energy and Banks drove the index, to which the Small-Mid portfolio has limited exposure. We believe the operating metrics of our portfolio companies are very favorable, and the strategy remains built for long-term durability.

Top 3 Contributors to Relative Performance

Entegris (ENTG) – ENTG outperformed its end markets and continued to gain share. Increased die size and a push to smaller nodes requires more wafer starts and more advanced contamination control, which are long term industry tailwinds. ENTG has drastically increased its size and scale while becoming one of the most diversified players in the semi-materials industry. The recent CMC Materials acquisition will further strengthen the company's competitive moat.

MBIA (MBI) – MBIA shares were strong all year. MBIA is no longer writing business, but is running off its book, which includes returning cash to shareholders via share repurchase. MBIA trades at a discount to adjusted book value and we believe it will continue to return excess capital to shareholders.

Martin Marietta (MLM) – MLM stock outperformed in 2021, largely driven by the passing of a new infrastructure bill. The $1 trillion bill reauthorizes key surface transportation programs for the next five years, significantly increasing highway funding over previous levels and providing greater visibility to the outlook for aggregates. Demand has also been driven by strength in industrial projects and single-family housing across the country.

Top 3 Detractors from Relative Performance

Citrix (CTXS) – A number of internal issues have negatively impacted CTXS in recent quarters including a shift to subscription based sales, a complicated technical selling process and activist led changes to management. CTXS products remain very relevant in cloud computing and work from home environments; meanwhile, margins are attractive and the balance sheet is solid.

Cannae Holdings (CNNE) – CNNE's underperformance in 2021 was the result of declines in the market value of its largest public holdings (Dun and Bradstreet, Ceridian, and PaySafe). The investment theses for its larger holdings remain intact, but some have taken longer to materialize than expected. Its SPAC investments have also been impacted by waning market sentiment for SPAC vehicles. CNNE trades at a discount to the fair value of its underlying investments, and we believe further upside will come from Foley's value creation efforts.

Lamb Weston (LW) – LW shares have been weak in recent months due to ongoing pandemic related challenges, particularly supply chain issues and inflationary costs (shipping and fertilizers). Making matters worse was a weak potato crop this year. Fortunately, volumes have recovered, but LW has not been able to pass through the higher costs yet, so margins are down. We think demand will remain strong, capacity utilization rates throughout the industry will bounce back leading to price increases, and margins for LW will rebound.

Portfolio Characteristics & Positioning

We believe the Small-Mid strategy is well positioned based on the strength of the companies owned and the overall quality characteristics of the portfolio—measured by sustainably high returns on capital and modest leverage. While the portfolio currently trades at a premium to the Value index, we believe this is justified as companies in the Value indexes have lower returns on capital and higher debt levels.

Portfolio Characteristics	Small-Mid Cap	Russell 2500 Value
Pre-tax ROC (3 yr. avg.%)	13.1%	6.7%
Net Debt/EBITDA	2.3x	3.2x
Enterprise Value/EBITDA	18.3x	12.6x

Source: FactSet

Looking Ahead

We remain positive regarding the economic outlook. As we enter 2022, we expect solid, but moderating economic growth. COVID remains a risk; but fortunately, the latest Omicron wave appears to be having less of an impact on the broader economy than prior variants. Meanwhile, inflation is still elevated, and the Fed is set to reverse accommodative monetary policy, which could further weigh on economic growth. In terms of the equity market, we recognize valuations are on the rich side, while interest rates will likely remain low vs. history.

The Fed is expected to begin increasing the funds rate later in 2022, but the increases will likely be in small increments. At current valuations along with various short term risks to the economic outlook (rising inflation, higher interest rates, potential tax increases), we expect greater volatility and possibly more muted returns in the near term. Given this backdrop, we believe a long term-approach, with a focus on Quality factors that may help dampen volatility, will reward investors.

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Annualized Returns
As of 12/31/2021

	QTD	1Y	3Y	5Y	10Y	ITD
Small-Mid Cap Gross	9.5%	20.7%	21.9%	14.6%	13.6%	17.1%
Small-Mid Cap Net	9.3%	19.8%	21.0%	13.7%	12.7%	16.2%
Russell 2500 Value	6.4%	27.8%	18.3%	9.9%	12.4%	15.0%

Inception date: 03/31/2009. Past performance should not be taken as a guarantee of future results.

Disclosure Notes

The London Company's performances are size weighted and annualized based on calculations for the period ending December 31, 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 Advisor, 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.

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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 U.S. 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.

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