Portfolio Commentary

Market Update

U.S. equities rallied during 4Q with the major indices posting double-digit returns. Moderating inflation, some weakening in the labor market, and slowing economic growth raised the odds of a soft landing. The easing of financial conditions combined with indications by the Federal Reserve that it would pivot to rate cuts later in 2024 set forth a positive feedback loop for risk assets in 4Q. For the quarter, the Russell 3000 Index rose 12.1%.

There was a notable broadening of market strength in 4Q, as Small and Mid-Cap stocks posted the strongest gains. The recent broadening out of the market was a welcome reprieve, yet the cap-weighted Large Cap indices remain historically top-heavy and the mega-cap Magnificent 7 (Apple, Microsoft, Amazon, NVIDIA, Alphabet, Tesla, & Meta Platforms) were dominant in 2023. Some of the biggest beneficiaries of the 4Q drop in yields were the biggest victims of the rise in yields: regional banks, property stocks, cyclical sectors, and low quality, highly levered companies. Looking at market factors, Volatility and Growth were positive in 4Q while Value and Yield factors were mixed. Quality and Momentum factors were the biggest detractors during the final quarter.

Key Performance Takeaways

The London Company Small Cap portfolio gained 11.9% (11.7% net) during the quarter vs. a 14.0% increase in the Russell 2000 Index. Sector exposure was a tailwind while stock selection was a headwind.

The Small Cap portfolio trailed its benchmark in 4Q, but finished in line with our goal of 85-90% upside capture. The portfolio's positive tilt toward Quality factors and limited exposure to regional banks were headwinds during 4Q. For the full year, however, the portfolio outperformed its benchmark, aided by the relative advantage of our Quality-orientation (sustainably high returns on capital & balance sheet strength).

Top 3 Contributors to Relative Performance

Armstrong World Industries (AWI) – AWI outperformed during 4Q after demonstrating earnings stability amidst a challenging demand backdrop, as well as strong progress on key growth initiatives. AWI's unique competitive advantages, diverse end market mix, and a favorable industry structure should support outperformance going forward.

Qualys (QLYS) – QLYS reported excellent 3Q23 earnings, showing another acceleration in bookings as well as solid margins. Additionally, the stock benefited from the rotation into growth in December, after dovish comments from the Fed. We have conviction the company should be able to return to its prior organic growth rates over time and still maintain their industry-leading profitability.

Atlantic Union (AUB) – AUB rallied during 4Q after reporting solid earnings. The bank has been quite active on many fronts, including the planned acquisition of a smaller bank in Southeast Virginia, solid execution on their cost reduction program, the sale-leaseback of several branch properties, and the restructuring of the securities portfolio in order to achieve much higher yields. Additionally, recent sentiment around banks ebbs and flows with the potential for Fed rate cuts, as higher rates are typically better for banks.

Top 3 Detractors from Relative Performance

Masonite (DOOR) – DOOR underperformed in 4Q after proposing an acquisition of PGT Innovations, a premium window and door manufacturer. DOOR's long-term capital allocation record is strong, and the management team has proven to be dutiful toward shareholders. We believe DOOR remains well positioned to capitalize on a very supportive demand backdrop, and the business's large market share and pricing power will support outperformance over the long term.

Cable One (CABO) – The market environment remains challenging for CABO with lower move activity and greater competition from fixed wireless offerings. Despite muted subscriber trends, CABO continues to generate profitable growth for its broadband service. Management appears disciplined in striking an appropriate balance between pricing and incremental penetration, while prioritizing free cash flow generation. CABO is well positioned as an advantaged provider of high-speed internet in rural markets. We believe its relatively low penetration, superior service, and M&A prowess are supportive of long-term earnings growth.

White Mountains (WTM) – We believe the relative underperformance of WTM in 4Q reflected dovish comments from the Fed and a rotation into more aggressive stocks. During the quarter, WTM launched a private investment fund led by John Daly, who founded Alleghany Capital (since Berkshire Hathaway acquired Alleghany and no longer needed a separate Alleghany Capital). We have confidence in management's ability to increase book value per share over time, through both conservative underwriting and portfolio changes.

Sector Influence

We are bottom-up stock pickers, but sector exposures influenced relative performance as follows:

- What Helped: Underweight Energy & Utilities (two weaker performing sectors)

- What Hurt: Underweight Health Care & Financials (two better performing sectors)

Trades During the Quarter

- Reduced: **Murphy USA (MUSA) & Tempur Sealy (TPX) –** Reductions reflect market cap constraints, which now exceeds $7B for TPX & MUSA. We trimmed on strength, and believe both companies remain well positioned for future growth.
- Exited: **LivaNova (LIVN) –** Sale reflects higher conviction in the new positions. LIVN is going through a transition to new leadership and faces strong competition from some of its larger med tech peers.
- Initiated: **ePlus (PLUS) –** PLUS specializes in providing IT solutions and optimizing organizations' IT and supply chain processes in the U.S. With a focus on the specialized IT sector, including data center infrastructure, networking, security, cloud, and collaboration, PLUS has gained market share in a fragmented reseller market. Prioritizing client tech spending areas has led to double-digit growth and industry-leading gross margins of about 24%, with EBIT margins at 8%. PLUS boasts a robust balance sheet with $20M in net cash, and we see potential for value appreciation, trading below conservative intrinsic value estimates.
- Initiated: **Revolve Group (RVLV) –** RVLV is an online-only fashion retailer targeting Millennial and Gen Z customers. Its site offers a curated selection of premium brands across apparel, footwear, accessories and beauty. Brand loyalty is strong, with net sales retention >90%. Customers appreciate the on-trend nature the curated selection, plus RVLV's ability to offer free, 2-day shipping and free returns is a differentiator versus peers. RVLV has increased revenue at +20%/year since its inception. ROIC has been steadily increasing and is roughly 50% today. RVLV is self-funding with a strong balance sheet (net cash of $270M), and has never used debt. In 2023, RVLV announced its first share repurchase program of $100M (~10% of market cap) to take advantage of the low stock price. Founded in 2003, the co-CEOs, hold 45% of the company.

Looking Ahead

After such a strong 2023, we believe investors should temper expectations for 2024. Stocks defied rate hikes, wars, collapsed banks, and recession fears in 2023. Now, calls for a soft landing are consensus; sentiment is overly optimistic; and markets are priced for very little risk. Predicting the future direction of the economy is always challenging. While we do agree the odds of a recession have come down, they are still elevated. A soft landing remains in reach, but much of that hinges on whether the Fed eases soon enough to avoid an employment problem. Perhaps this time it will be different, but historically the odds of sticking the landing have been very low. Even though we have greater clarity over the Fed's path from here, there still remains a long list of items creating uncertainty that could lead to greater volatility in 2024.

In terms of the equity market, we believe returns in the near term may be modest, with shareholder yield (dividends, share repurchase, debt reduction) comprising a significant percentage of the total return. Economic growth is likely to slow; earnings estimates appear optimistic; and valuations are somewhat elevated. Moreover, investors continue to expect a faster pace of rate cuts than members of the FOMC currently suggest. The difference in the pace of rate reductions could lead to greater levels of volatility in 2024. Markets are impossible to outguess in the short run, but we believe the antidote to uncertainty is quality and that solid company fundamentals will lead to strong risk-adjusted returns in the long run. With that in mind, the characteristics of our portfolios remain attractive, and we believe we're well positioned for an uncertain future.

Annualized Returns
As of 12/31/2023

	QTD	1Y	3Y	5Y	10Y	ITD
Small Cap (Gross)	11.9%	22.0%	10.3%	14.0%	7.1%	12.5%
Small Cap (Net)	11.7%	21.2%	9.5%	13.2%	6.3%	11.9%
Russell 2000	14.0%	16.9%	2.2%	10.0%	7.2%	8.1%

Inception date: 9/30/1999. Past performance should not be taken as a guarantee of future results.
Performance is preliminary. Subject to change.

Disclosure Notes

The London Company's performances are size weighted and annualized based on calculations for the period ending December 31, 2023. 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.

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Composite Creation/Inception Date: September 30, 1999

Composite Definition: The Small Cap strategy invests mainly in conservative, low-beta, small-cap equities with a focus on above-average downside protection. Primarily we seek profitable, financially stable small-cap companies that consistently generate free cash flow, high returns on unleveraged operating capital, trade at significant discounts to their intrinsic values, and are run by shareholder-oriented management. Positions are usually within the market capitalization range of the major, domestic small-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 2000 Index and has a creation and inception date of September 30, 1999. 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. As of July 1, 2022 The London Company redefined the composites to exclude all dual contract relationship and any potentially bundled fee scenarios. This policy is not retroactive, but will continue to apply going forward.

Benchmark Description: Primary: Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. Russell 2000 is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. Secondary: Russell 2000 Value Index measures the performance of the small-cap segment of the U.S. equity universe. It includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. Benchmark returns are not covered by the report of independent verifiers.

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. 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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The London Company of Virginia, LLC

1800 Bayberry Court, Suite 301
Richmond, VA 23226

Tel: 804.775.0317
info@TLCadvisory.com

www.TLCadvisory.com