

Portfolio Commentary

Market Update

U.S. stocks posted mixed results during 2Q24. The broader market, measured by the Russell 3000 Index, rose 3.2% with gains concentrated in large companies with ties to spending on artificial intelligence. The S&P 500 reached new all-time highs during the quarter, but market breadth (a measure of how many stocks are participating in the rally) sharply declined once again. The Russell 2000 Small Cap Index was down 3.3%. Economic data released during the quarter reflected decelerating growth, some weakening in the labor market, and lower inflation, which collectively support the notion of rate cuts beginning in the next few months. Corporate earnings were solid, but there were signs of greater caution from consumers. Investors continued to favor Large Cap, Growth and Momentum factors, consistent with trends in recent quarters. Value and Yield factors continued to face headwinds, while Quality & Volatility had a mixed impact.

Key Performance Takeaways

The London Company Income Equity portfolio declined 1.6% (1.7% net) during the quarter vs. a 3.6% increase in the Russell 1000 Index. Sector exposure and stock selection were both headwinds to relative performance.

The Income Equity portfolio came up short of our 85-90% upside capture expectations during the quarter. Our approach faced headwinds as Momentum and Growth factors continue to lead, and the factors we emphasize, such as Quality, lower Volatility, & Yield remain out of favor. Narrow breadth and the concentrated weight of the growth-oriented mega caps presented obstacles. The opportunity cost from underexposure to the Magnificent 7 stocks was significant, as these stocks contributed over 100% of the return of the Russell 1000 Index for 2Q.

In today's momentum-driven market, the line between short-term bets and long-term investments has become increasingly blurred, making it more crucial than ever to distinguish between chasing short-term gains and investing for long-term wealth creation.

Top 3 Contributors to Relative Performance

Texas Instruments (TXN) – TXN rallied in 2Q despite declining revenue in its latest update. TXN is beginning to see some encouraging signs of destocking nearing an end and some sub-segments of the market are experiencing improving demand. TXN continued to spend on capex and should begin to see positive benefits to cash flow next year from the CHIPS Act.

Philip Morris (PM) – Shares rallied in 2Q after muted performance to start the year. The smoke free category continues to be the primary driver with notable strength from ZYN nicotine pouches. IQOS growth has been fueled by ongoing innovation and smoker conversions, while the US

remains a large and untapped commercialization opportunity on the horizon. Successful execution of the portfolio transition has resulted in smoke-free products now contributing nearly 40% of total net revenues and gross profit. Guidance suggests a continued acceleration in the adoption of reduced-risk products, which will drive overall volume growth and market share gains. We believe that the growth potential of the smoke-free category combined with a resilient and profitable combustibles portfolio will lead to significant and sustainable free cash flow generation.

Air Products (APD) – We added to our position in APD this year and the stock subsequently outperformed during 2Q. APD continually posts results for its base business comparable to that of its closest industrial gas peers, and margins have recovered back towards industry-leading levels. We believe the offtake announcement in June between APD and TotalEnergies for 30% of NEOM's green hydrogen output is a good first step towards alleviating investor concerns about the return profile for clean energy megaprojects.

Top 3 Detractors from Relative Performance

Norfolk Southern (NSC) – NSC pre-announced weaker results in early April. Revenue declined in its latest quarter driven by lower fuel surcharges, an unfavorable product mix, and lower intermodal ancillary fees. Costs continued to rise. Activist involvement may lead to lower costs in the future.

Lowe's (LOW) – LOW underperformed as sales at the company were negatively affected by falling do-it-yourself spending from consumers. Sales to Pro customers remained positive. Decelerating consumer spending and weaker housing data is likely weighing on results at LOW. On a positive note, consumers staying in their homes due to higher interest rates and the aging of homes around the country is typically a positive for home improvement spending.

Fastenal (FAST) – After a strong start to the year, FAST underperformed during 2Q due to sluggish broad-based demand, and a slowdown in customer acquisition. FAST is delivering on its various growth drivers, including on-site signings ahead of target, increasing e-commerce and digital footprint sales, and ongoing growth in Fastenal Managed Inventory signings. Despite the slowdown in its end markets, FAST's balance sheet remains in good shape and its cash generation is strong. FAST's counter-cyclical free cash flow profile is appealing in the current economic environment and provides ample downside protection.

Sector Influence

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

- What Helped: Underweight both Health Care & Consumer Discretionary (weaker performing sectors)
- What Hurt: Underweight Info. Technology (a better performing sector) & overweight Financials (a weaker performing sector)

Trades During the Quarter

- Reduced: **Fastenal (FAST)** - Trimmed position following recent strength in shares. There's no change to our long-term thesis.
- Increased: **Nestle (NSRGY)** - Added to position following recent weakness in the shares. There is no change in the thesis for either holding, but we note that NSRGY trades at an attractive valuation and recent insider purchases gives us greater conviction in the timing of the additions
- Increased: **Nintendo (NTDOY)** - Addition reflects our positive long-term outlook for the business and our desire to reduce cash in the portfolio.
- Exited: **Verizon (VZ)** - Sale reflects heightened competitive activity from both AT&T and T-Mobile. While VZ has the highest quality network, we are concerned that its competitors' focus on market share gains could continue to negatively affect VZ's business, resulting in both lower margins and returns on capital.
- Initiated: **TE Connectivity (TEL)** - TEL designs and manufactures connectors and sensors, supplying solutions to the transportation, industrial, and communications industries. The critical components that TEL sells have long life cycles and they make up a small percent of the overall cost of materials for a complex electronic systems (i.e. low cost but high-cost failure products), creating high switching costs and barriers to entry. TEL has leading share in the global connector market (including 30-35% share in automotive) with leverage to secular growth from the 'electrification' of multiple end markets. TEL's management team has enacted successful cost-realignment strategies, driving significant margin improvement and leading to mid-teens returns on invested

capital. TEL fits our process well. It has a low level of net debt, generates healthy cash flows, returns a significant amount of capital back to shareholders through its dividend and buyback program, and it currently trades at a discount to our estimate of intrinsic value and a discount to its peers. Given its strong competitive position, capital allocation philosophy, and favorable industry tailwinds, we believe TEL presents an opportunity to own a high quality compounder.

Looking Ahead

Conditions are trending in a positive direction for the Fed to begin reducing rates. Inflation is still higher than the Fed's target, but it has continued to drift lower. The labor market remains strong, but there have been some signs of weakening. Together with signs of weakness in some recent economic data, we could see the Fed shift to a less restrictive policy and reduce rates before year-end. While the odds of a recession in the near term have declined, risks remain. Longer term, we remain positive regarding the U.S. economy and expect real annualized GDP growth in the 1.5-2% range driven by growth in the labor force and improving productivity.

In terms of equities, we note that narrow, top-heavy markets are fragile markets. The odds of a recession have come down, but our cautious posture persists due to high valuations, market concentration, looming debt challenges, and the lengthiest inversion of the yield curve in history. Continued multiple expansion in a higher rate environment is unlikely. We suspect the S&P 500 will eventually track earnings, so we would expect more volatility, especially in stocks where a lot of growth is already priced in. 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. In our view, this uncertain economic backdrop warrants an investment approach that prioritizes consistency and stability—not excessive wagers. Owning great businesses at reasonable prices and allowing them to compound is still a winning, long-term strategy.

Annualized Returns

As of 6/30/2024

	QTD	YTD	1Y	3Y	5Y	10Y	ITD
Income Equity (Gross)	-1.6%	4.0%	6.2%	2.6%	8.2%	8.9%	8.9%
Income Equity (Net)	-1.7%	3.8%	5.8%	2.2%	7.8%	8.4%	8.3%
Russell 1000	3.6%	14.2%	23.9%	8.7%	14.6%	12.5%	7.6%

Disclosure Notes

The London Company's performances are size weighted and annualized based on calculations for the period ending June 30, 2024. 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.

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Composite Creation/Inception Date: December 31, 1999

Composite Definition: The Income Equity strategy invests mainly in common equities with a focus on higher overall dividend yield orientation, which may be supplemented with primarily investment grade, preferred equities. This strategy has a more conservative orientation, with a focus on capital preservation, income and growth, in order to provide greater yield and downside protection relative to our Large and Mid Cap strategies. Our Income Equity strategy is designed to generate above-average, absolute returns over full market cycles. Accounts in this product composite are fully discretionary taxable and tax-exempt portfolios with no minimum dollar amount of assets. The product is measured against the Russell 1000 Value Index and has a creation and inception date of December 31, 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 relationships and any potentially bundled fee scenarios. This policy is not retroactive, but will continue to apply going forward.

Benchmark Description: The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 Index companies with lower price-to-book ratios and lower expected growth values. Benchmark returns are not covered by the report of independent verifiers. The Income Equity product is typically compared to the Russell 1000 Value Index. Any comparison to the Russell 1000, S&P 500 or their corresponding ETFs, 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 London Company 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. Prior to April 1, 2024 returns are calculated gross of withholding taxes on foreign dividends and interest. Starting April 1, 2024, performance is calculated net or gross of foreign withholding taxes on dividends and interest income dependent on custodian data. Dividends are reinvested. The accounts represented in the composite reflect actual London Company fees paid on the particular account which may be different from the fee normally offered to other clients. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

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