

# Portfolio Commentary

## Market Update

U.S. equities traded higher during Q3 with most of the major indices posting mid-single digit gains. The quarter was marked by significant market shifts, including inflation cooling, employment weakening, volatility spiking, and a larger-than-expected Federal Reserve rate cut, yet the stock market ended on a high note. The broader market, measured by the Russell 3000 Index, rose 6.2%. There was a notable rotation to small cap and value styles away from large cap growth. This fostered broader market participation, with a wider range of sectors participating, especially the rate sensitive areas. Looking at market factors, Yield and most Value factors posted the strongest returns while most of the Growth, Volatility, and Momentum factors presented headwinds. Quality factors had a mixed impact.

## Key Performance Takeaways

The London Company Small-Mid Cap portfolio returned 2.2% (2.0% net) during the quarter vs. a 8.8% increase in the Russell 2500 Index. Both sector allocation and stock selection were headwinds to relative performance.

The SMID portfolio trailed its benchmark and came up short of our 85-90% upside capture expectations during 3Q. The portfolio didn't fully benefit from the rotation away from mega-cap growth stocks. The areas of the market that rallied the most were lower-quality, highly leveraged companies, which stand to benefit the most from rate reprieve. Our focus on balance sheet strength, which typically benefits us, became a temporary headwind. Another challenge was being underweight rate-sensitive sectors (e.g. Real Estate, Comm. Services & Utilities), which were the best-performing sectors down-cap. Lastly, idiosyncratic weaknesses in a few holdings were a drag on performance in a robust return environment. While the short-term report card hasn't been as favorable this year as the prior two, the longer term performance remains strong.

## Top 3 Contributors to Relative Performance

**Waters Corporation (WAT)** – Shares of WAT rallied during 3Q as demand trends improved while results in China were better than expected. WAT continues to launch new products into higher growth verticals, which should lead to revenue growth and longer-term margin expansion. On the capital allocation front, management comments suggest a likely resumption of share buybacks in the future, and the contribution from the Wyatt acquisition has been better than expected.

**Zebra Technologies Corporation (ZBRA)** – ZBRA reported strong operating results, reflecting better-than-expected customer demand and strong execution. While management is not calling for an inflection in customer sentiment yet, expectations were low going into the quarter, so the stock rallied. While we have no clear visibility on the timing of a rebound, we think the company is well-positioned to

strengthen its market position and rapidly increase margins coming out of the current tepid demand environment. We continue to have confidence in the quality of the business and competence of management.

**Armstrong World Industries, Inc. (AWI)** – Shares of AWI have been strong over the last two years. AWI maintains leading market share in ceiling tiles at 55% (competes with USG and CertainTeed). The company serves a diverse group of end markets. Sales in the most recent quarter rose over 12%. Long-term contracts with distributors and warranties on the installed base (which require contractors to use original manufacturers) are advantages that should help AWI in the future.

## Top 3 Detractors from Relative Performance

**Entegris, Inc. (ENTG)** – ENTG lagged the broader market during 3Q due to a more gradual recovery for trailing edge nodes, slower wafer starts, and delayed manufacturing capex spending. The near-term market conditions and different recovery rates throughout the industry have led to a more cautious outlook for the remainder of the year. That said, its solutions for advanced technology and incremental wafer content gains should propel a faster recovery next year. ENTG is one of the most diversified players in the semi-materials industry with its size and scale. We remain attracted to the industry's high barriers to entry, limited competitors, and high switching costs.

**Lamb Weston Holdings, Inc. (LW)** – LW underperformed this quarter due to the residual effect from its ERP (Enterprise Resource Planning) rollout issues, market share losses, and limited visibility on a recovery in demand. The broad-based volume slowdown and higher fixed-cost nature of the business have muted margins. Management has taken action to fix what it can control by taking out costs, increasing productivity, and removing less efficient capacity. We remain attracted to LW's market share, flexible balance sheet, and long-term industry tailwinds.

**White Mountains Insurance Group Ltd. (WTM)** – Shares of WTM underperformed the market during 3Q. The company generates much of its income from P&C insurance, and the stock tends to track growth in book value over time. Separately, WTM has a good track record of creating value via capital allocation (buying and selling businesses) decisions, so transactions like the sale of NSM and also movements in its underlying investments (e.g. MAX) can meaningfully impact shares. We remain confident in management's ability to deliver outsized growth in book value per share over time through prudent capital allocation.

## Sector Influence

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

- What Helped: Underweight Energy & Information Technology (two weaker performing sectors)
- What Hurt: Underweight Financials (a better performing sector) & overweight Cons. Staples (a weaker performing sector)

## Trades During the Quarter

- There were no trades during the quarter.

## Looking Ahead

Stocks enter 4Q in good form, but challenges remain. The market appears priced for near perfection, with expectations of a soft landing and healthy earnings growth driving the S&P 500 to a lofty valuation that leaves little room for error. The Fed's recent rate cut may sow the seeds for a cyclical recovery, but whether the economic impact arrives in time to avoid a downturn is uncertain. Lower rates tend to support market sentiment and multiples in the short term, but it can take up to two years for policy changes to impact economic and earnings data. Meanwhile, rates remain in restrictive territory. Therefore, the impact of restrictive policy may continue to affect the economy in the months ahead. While we believe that the odds of a near term recession are low, we note the difficulty in navigating a soft landing.

In terms of the equity market, valuations based on near term earnings are elevated in the context of moderate GDP growth. We believe that equity returns in the near term may be modest, with shareholder yield (dividends, share repurchase, debt reduction) comprising a significant percentage of the total return from equities. Moreover, as a large corporate debt maturity wall approaches, balance sheet strength will likely become a differentiator and an advantage for investors focused on fundamentals. We believe our focus on quality, diversification, and valuation will continue to reinforce our margin of safety, positioning our portfolios for success in this uncertain climate.

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## Annualized Returns

As of 9/30/2024

	QTD	YTD	1Y	3Y	5Y	10Y	ITD
SMID Cap (Gross)	2.2%	5.4%	21.4%	7.5%	10.0%	9.4%	14.8%
SMID Cap (Net)	2.0%	4.8%	20.5%	6.7%	9.2%	8.6%	13.9%
Russell 2500	8.8%	11.3%	26.2%	3.5%	10.4%	9.5%	13.9%

Inception date: 3/31/2009. 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 September 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 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:** 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. As of July 1, 2022 The London Company redefined the composites to exclude dual contract relationships and any potentially bundled fee scenarios. This policy is not retroactive, but will continue to apply going forward.

**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.

**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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