Value Investing:
Poking Holes in the Popular Narrative

Lyrical U.S. Value Equity
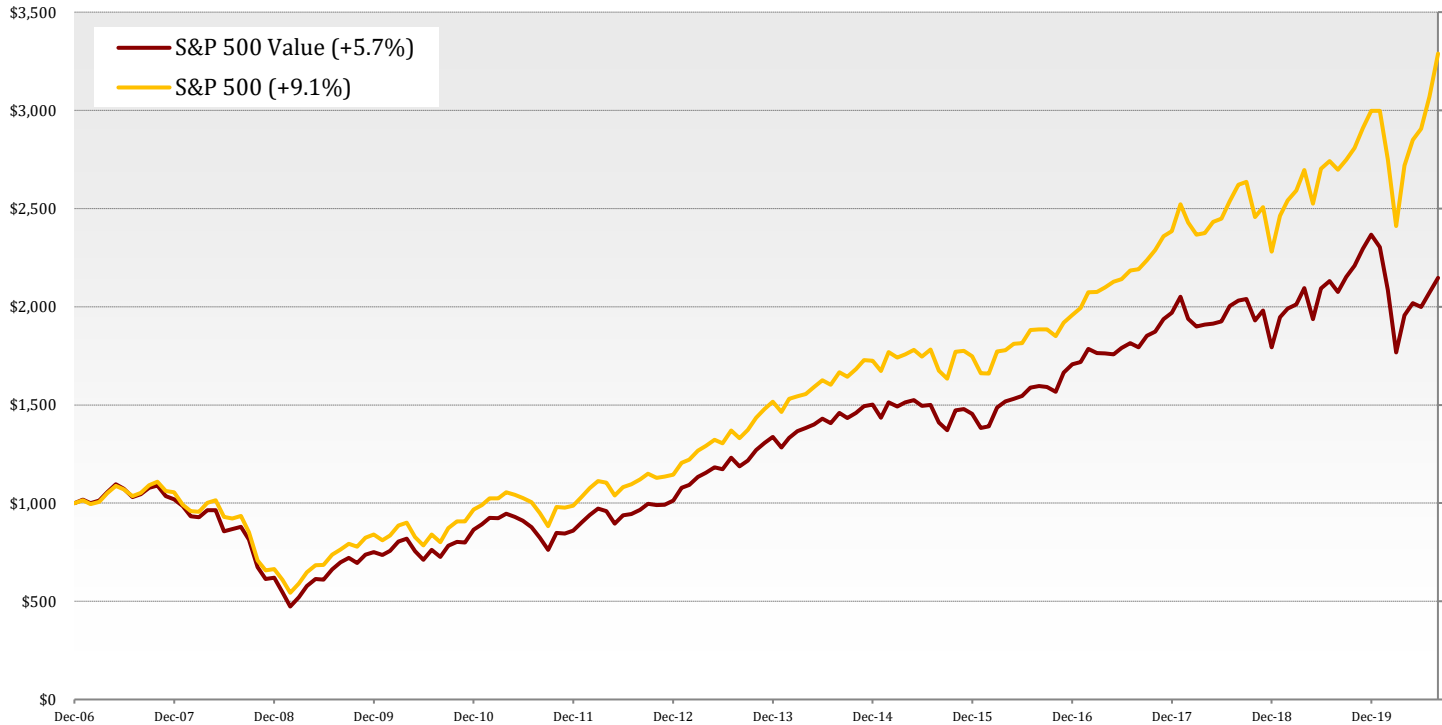
September 10, 2020

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New York, NY 10019
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S&P 500 Value index has underperformed for more than a decade

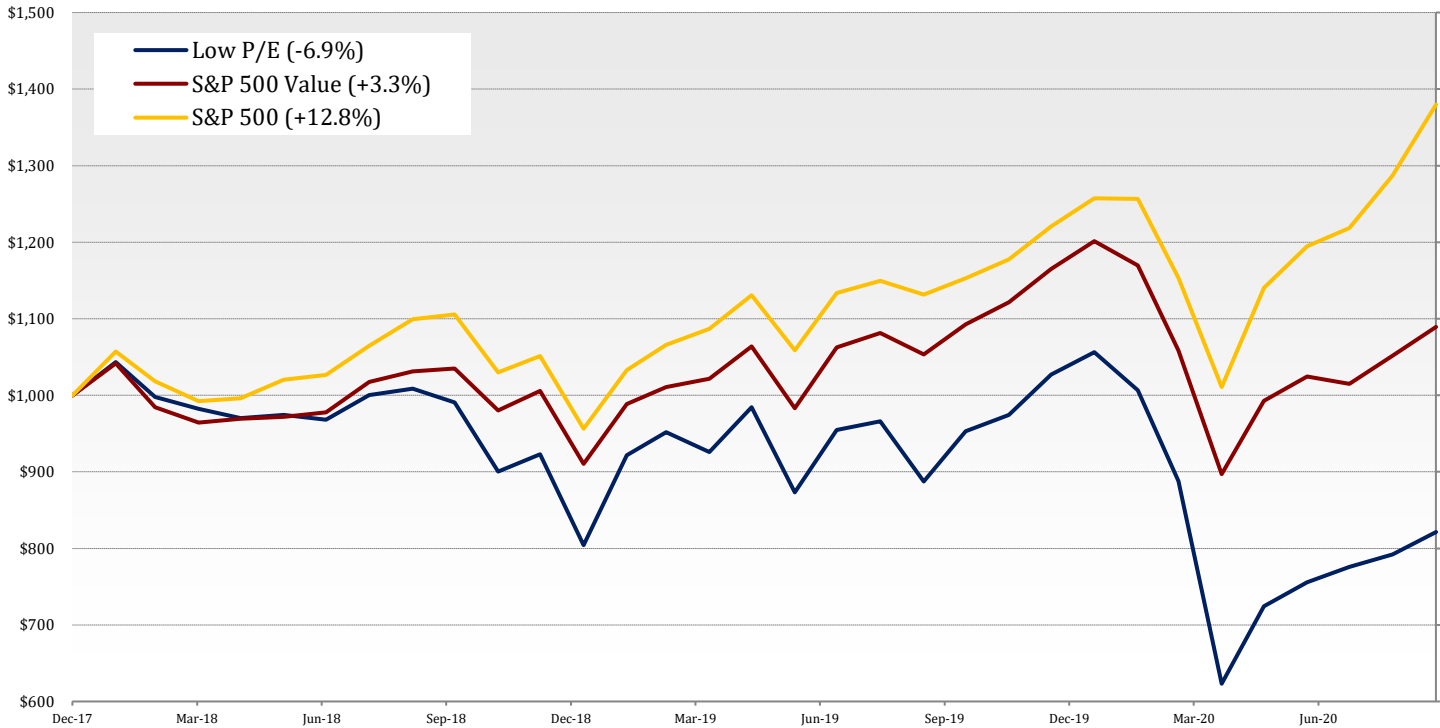## Growth of $1,000: January 2007 – August 2020

Legend:
- S&P 500 Value (+5.7%)
- S&P 500 (+9.1%)

See Performance Notes. Past performance is not necessarily indicative of future results.

Yet, value <u>stocks</u> outperformed even as the value <u>index</u> did not

Growth of $1,000: January 2009 – December 2017

Legend:
- Low P/E (+19.3%)
- S&P 500 Value (+13.7%)
- S&P 500 (+15.3%)

See Performance Notes. Past performance is not necessarily indicative of future results.

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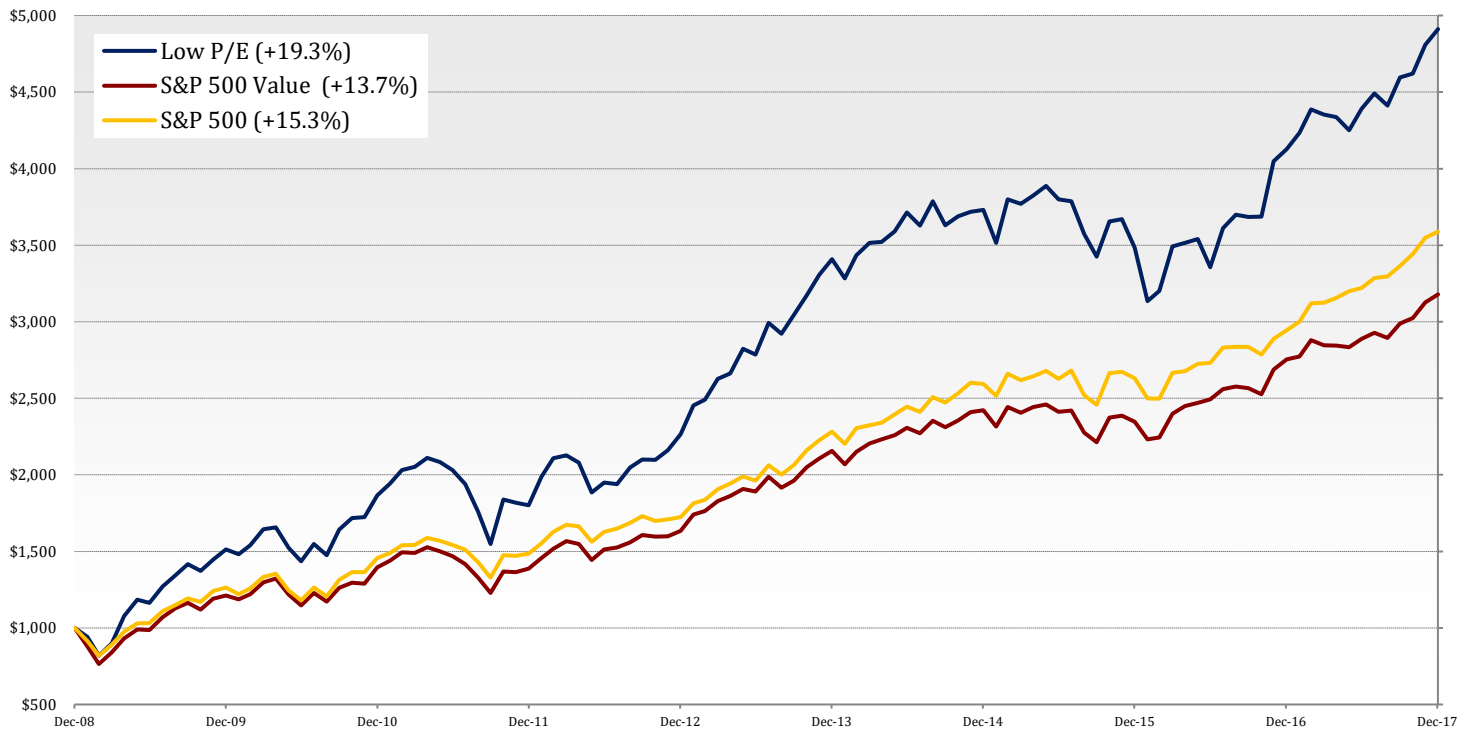
Value stocks have only been underperforming since 2018

Growth of $1,000: January 2018 – August 2020

Legend:
- Low P/E (-6.9%)
- S&P 500 Value (+3.3%)
- S&P 500 (+12.8%)

See Performance Notes. Past performance is not necessarily indicative of future results.

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You Can't Get Value From the Value Index

	Low P/E Quintile	S&P 500 Value
Selection Universe	1000 Largest Stocks	S&P 500
# of Holdings	200	395
Value Factor	P/E (NTM)	P/B, P/E & P/S
Growth Anti-Factor	None	EPS, Sales & Momentum
Weighting	Equal Weighted	Capitalization Weighted
Passive Share (S&P 500)	12%	62%
Cum. Return ('98 – '20*)	+732%	+301%
Cum. Rel. Return ('98 – '20*)	+279%	-153%

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Most stocks in SP500V are not in cheapest quintile

2009 -2017

S&P 500 Value by NTM P/E Quintile

Pie chart values:
- Priciest, 15.6%
- Cheapest, 25.9%
- Cheap, 22.1%
- Median, 19.5%
- Pricey, 16.9%
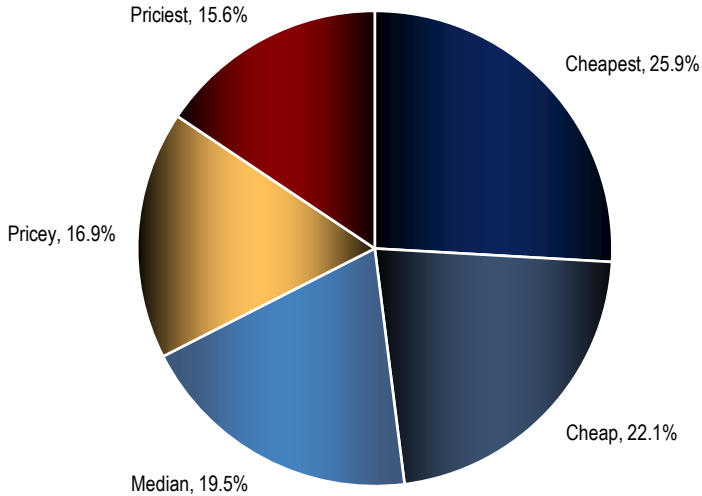
Annualized Return by NTM P/E Quintile

Bar chart legend: Lyrical Universe, SP500V, S&P 500

- Cheapest: 19.6%, 20.4%
- Cheap: 18.0%, 18.0%
- Median: 18.1%, 15.5%
- Pricey: 14.4%, 15.6%
- Priciest: 15.3%, 15.0%
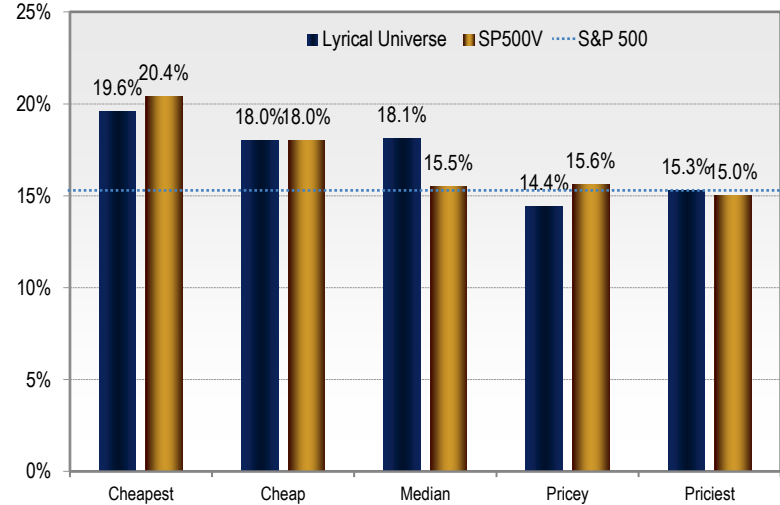
Capitalization weighting hurts value stock returns

2009 -2017

S&P 500 Value by NTM P/E Quintile

Priciest, 8.5%
Pricey, 14.6%
Median, 18.8%
Cheapest, 34.8%
Cheap, 23.3%
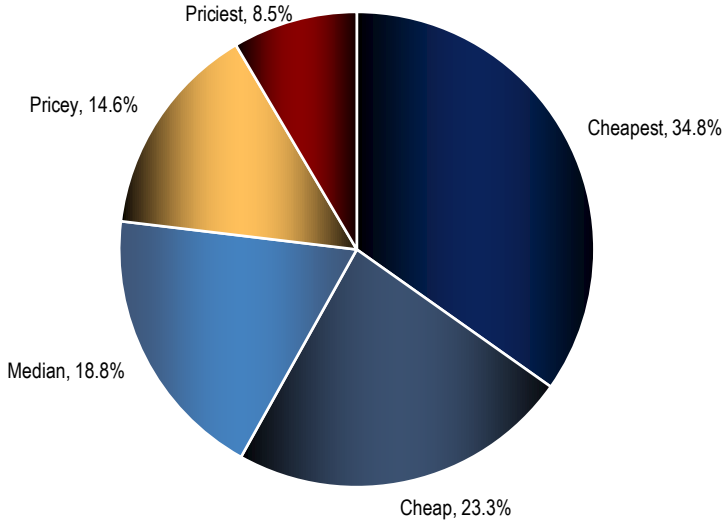
SP500V Cap Weight vs. Equal Weight Return

Category	Return
Cheapest	-5.6%
Cheap	-4.8%
Median	-3.5%
Pricey	-2.3%
Priciest	-1.0%

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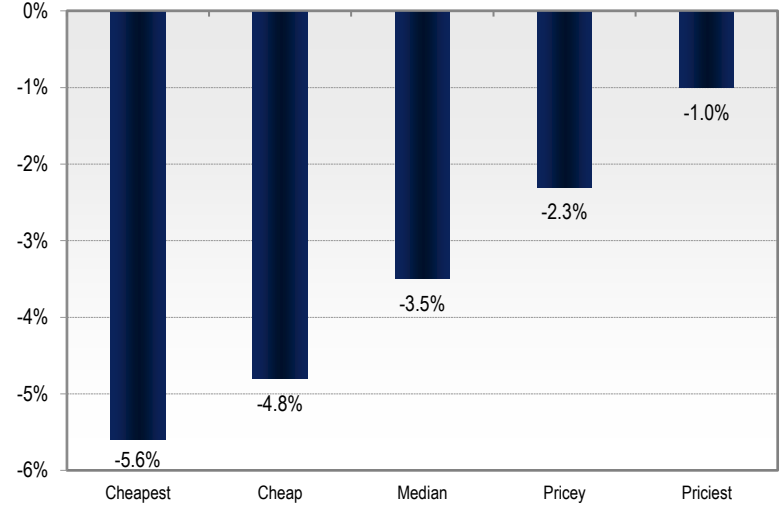
Performance Attribution of SP500V vs. Cheapest Quintile

2009 -2017

Cheapest Quintile	Allocation Effect	SP500V Equal Weight	Cap Weighting	SP500V Cap Weighted
19.6%	-2.3%	17.3%	-3.7%	13.6%

S&P 500: 15.3%

Disclaimer: Data shown for period from 2009-2017

Why Value Stocks?

Growth of $1,000

Legend:
- Cheapest Quintile
- S&P 500
- S&P 500 Growth
- S&P 500 Value

+450 bps
Annualized outperformance of cheapest quintile over S&P 500

+169%
Avg. cumulative 10-year outperformance of cheapest quintile over S&P 500

94%
Frequency with which cheapest quintile has outperformed S&P 500 over 10 years

0
Number of times the cheapest quintile has produced a loss over 10 years

8.3 Years
Avg. length of outperformance upcycle for cheapest quintile

1.8 Years
Avg. length of underperformance downcycle for cheapest quintile

Y-axis: $0, $50,000, $100,000, $150,000, $200,000, $250,000, $300,000, $350,000, $400,000, $450,000, $500,000

X-axis: Dec-78, Dec-80, Dec-82, Dec-84, Dec-86, Dec-88, Dec-90, Dec-92, Dec-94, Dec-96, Dec-98, Dec-00, Dec-02, Dec-04, Dec-06, Dec-08, Dec-10, Dec-12, Dec-14, Dec-16, Dec-18

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Please refer to Important Notes with respect to this and subsequent slides.

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History of Value Performance Cycles

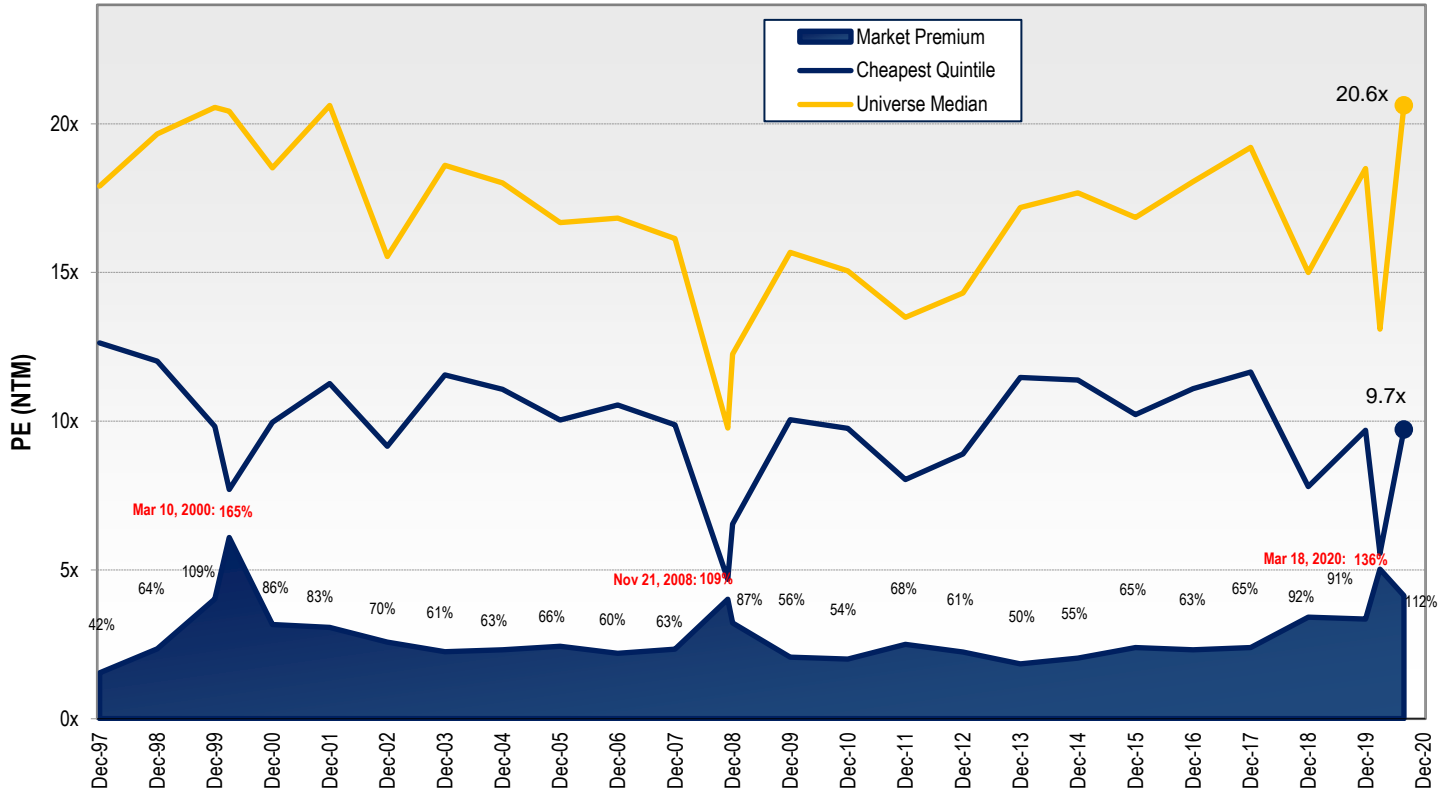| Start	End	Length (Yrs)	Cumulative			Annualized		
			Cheapest Quintile	S&P 500	Delta	Cheapest Quintile	S&P 500	Delta
Jan-60	Feb-71	11.2	477.9%	213.4%	+264.5%	17.0%	10.8%	+6.2%
Mar-71	Jun-73	2.3	-4.4%	16.3%	-20.7%	-1.9%	6.7%	-8.6%
Jul-73	Jul-79	6.1	206.4%	30.4%	+176.0%	20.2%	4.5%	+15.7%
Aug-79	Nov-80	1.3	17.4%	45.6%	-28.3%	12.8%	32.6%	-19.8%
Dec-80	Aug-89	8.8	606.0%	261.8%	+344.2%	25.0%	15.8%	+9.2%
Sep-89	Oct-90	1.2	-32.8%	-10.0%	-22.8%	-28.9%	-8.6%	-20.3%
Nov-90	Dec-97	7.2	544.5%	286.6%	+257.9%	29.7%	20.8%	+8.9%
Jan-98	Feb-00	2.2	-13.4%	45.0%	-58.4%	-6.4%	18.7%	-25.1%
Mar-00	Jun-07	7.3	402.4%	24.1%	+378.3%	24.6%	3.0%	+21.6%
Jul-07	Nov-08	1.4	-55.5%	-38.5%	-17.0%	-43.5%	-29.1%	-14.5%
Dec-08	Dec-17	9.1	434.2%	262.6%	+171.6%	20.3%	15.2%	+5.0%
Jan-18	Mar-20	2.3	-37.7%	1.1%	-38.8%	-19.0%	0.5%	-19.4%
Total Period		**60.3**	**391,624%**	**35,257%**	**+356,367%**	**14.7%**	**10.2%**	**+4.5%**
Average Up Cycle		**8.3**	**427.8%**	**152.2%**	**+275.6%**	**22.3%**	**11.8%**	**+10.5%**
Average Down Cycle		**1.8**	**-24.8%**	**5.4%**	**-30.2%**	**-14.8%**	**3.0%**	**-17.8%**

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Strength of Upcycle Does Not Correlate to Strength of Downcycle
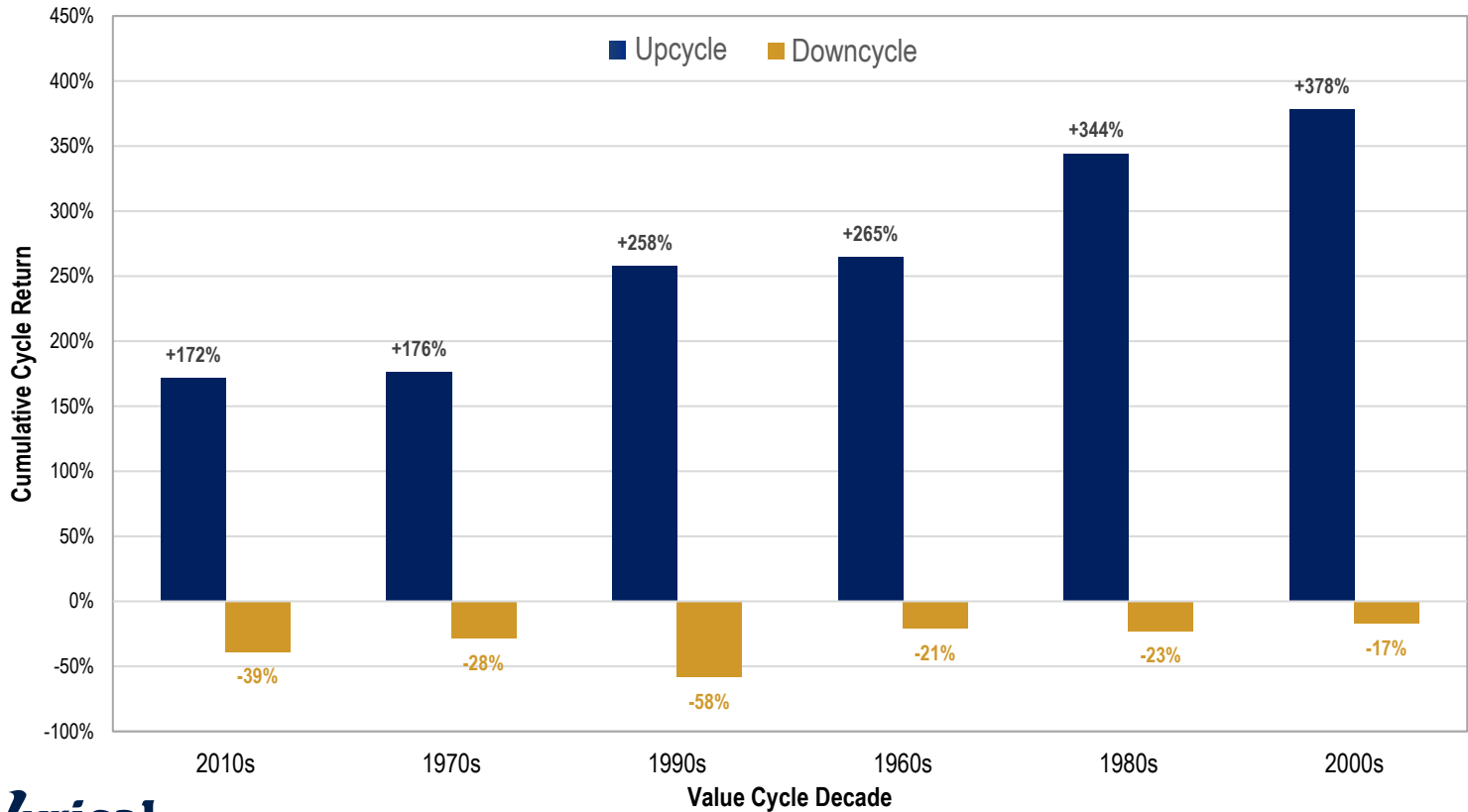
Worse Down Cycles Have Led to Better Upcycles

Cumulative Cycle Return vs **Value Cycle Decade**

Legend: Downcycle (gold), Upcycle (blue)

Value Cycle Decade	Downcycle	Upcycle
2010s	-17%	+172%
1970s	-21%	+176%
1990s	-23%	+258%
1980s	-28%	+344%
2020s	-39%	???
2000s	-58%	+378%

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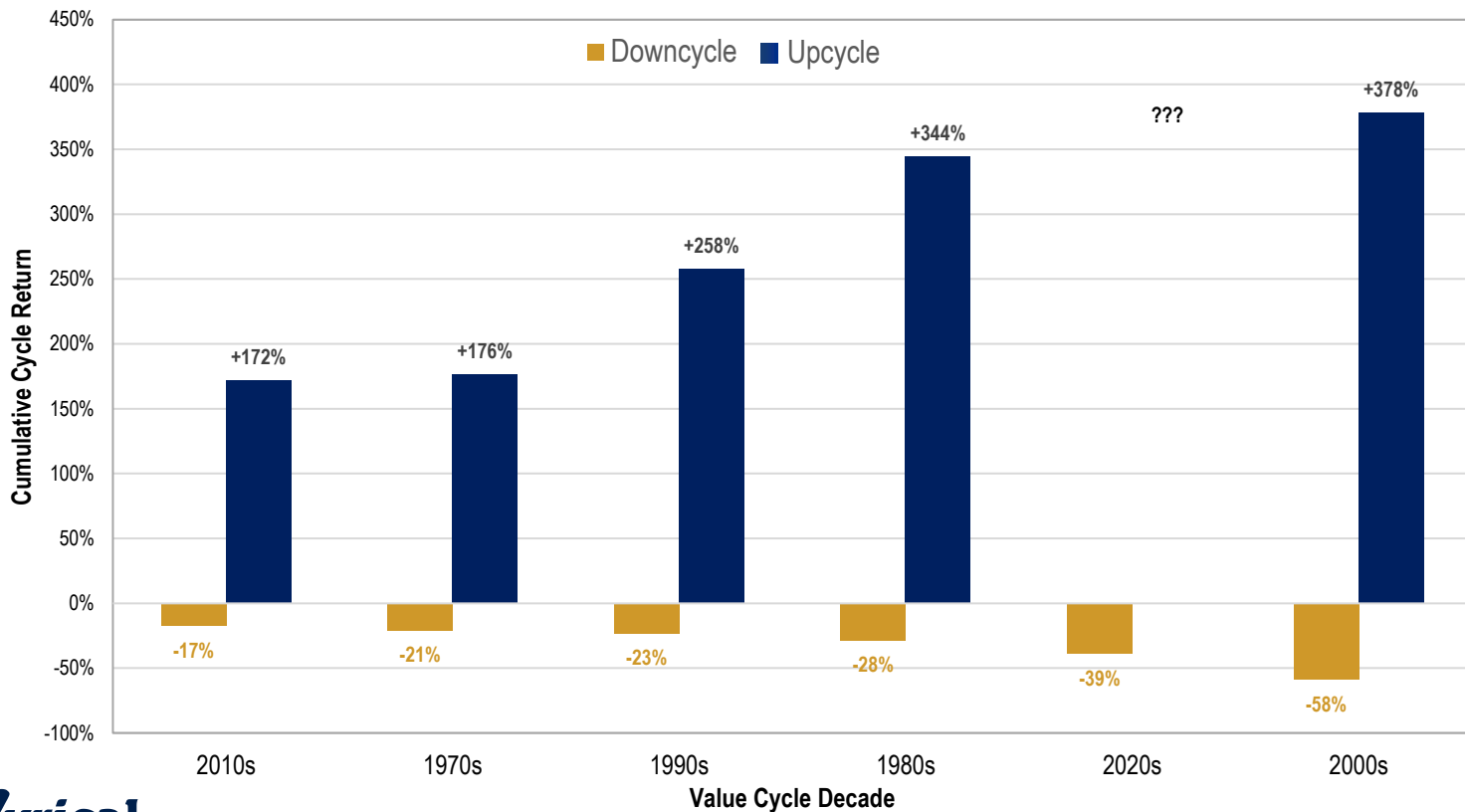
Valuation spreads are extreme by historical standards

Valuation spreads are extreme by almost every measure

Value Spreads, Equal-Weighted Top 1000 Stocks, Industry-Neutral December 31, 1967 – March 31, 2020*			
Value Spread Measure	**Current Percentile**	**(Current – Median) / (Max – Median)**	**Current STD Event**
Price-to-Book	100%	100%	+4.2
Price-to-Sales	99%	75%	+2.7
Price-to-Earning (trailing)	100%	100%	+3.1
Price-to-Earnings (forecast)	100%	100%	+5.5
Composite	100%	100%	+5.0

Composite Value Spreads, Equal-Weighted Top 1000 Stocks, Industry-Neutral December 31, 1967 – March 31, 2020**			
What's Removed	**Current Percentile**	**(Current – Median) / (Max – Median)**	**Current STD Event**
Nothing Removed	100%	100%	+5.0
Remove Tech / Telecom / Media Industries	100%	100%	+5.1
Remove 5% Mega Caps*	100%	100%	+5.4
Remove 10% Most Expensive Stocks	100%	100%	+5.0

Note: Using only the largest 1000 US stocks.
* Forecasted Price-to-Earnings starts January 31, 1976
** Composite value spread uses four signals: Price-to-Book, Price-To-Sales, Price-to-Earnings (trailing), and Price-to-Earnings (forecasted). This portfolio ois industry-neutral and equal-weighted using the largest 1000 stocks
*** Reported here is the composite over all four measures. If we remove the mega-caps within each industry and do the composite over the other three measures excluding forecasted price-to-earnings you get 100%, 100%, +4.7 STD.
Source: AQR (Is (Systematic) Value Investing Dead? May 8, 2020), CRSP, XPressFeed.

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The Lyrical Way is V-Q-A
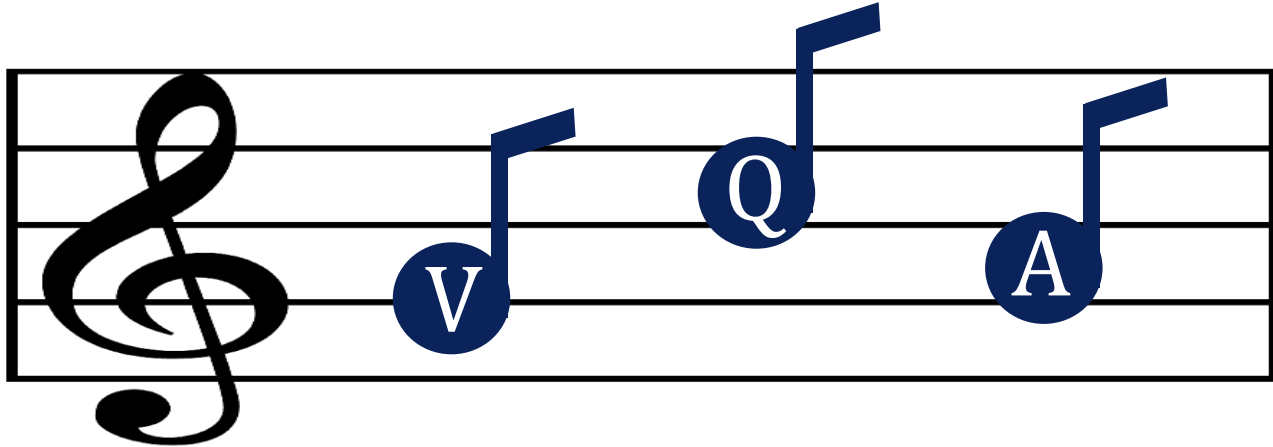
Value

Value investing is the best way we know to generate superior long-term returns.

Not just value investing, but **deep value** investing. The deeper the discount, the greater the return (when you're right).

The challenge is separating companies that deserve low valuations from those that don't.

Quality

In our experience, avoiding low ROIC companies improves the probability of success.

Among the cheapest stocks, we only invest in companies with an expected ROIC >10%.

We avoid certain industries because they do not meet our ROIC hurdle:
- Deep Cyclicals (e.g., Airlines)
- Basic Materials
- Regulated Utilities

Analyzability

In our experience, the easier it is to analyze a business, the greater the probability of success.

Some businesses are too complex or opaque to analyze adequately.

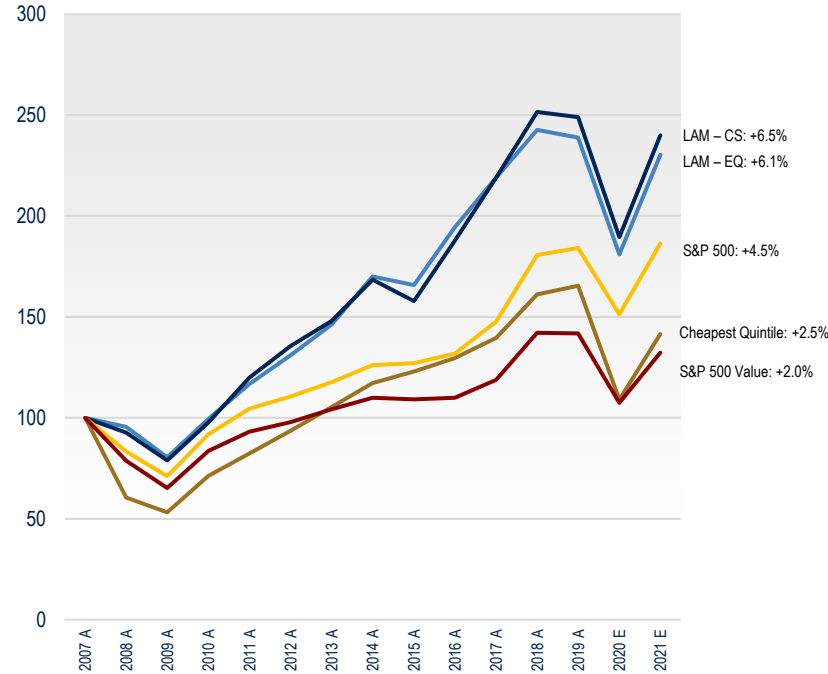We avoid certain industries because they lack analyzability:
- Banks
- Pharma / Biotech
- Traditional Retail

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Uncommon Combination of Deep Value <u>and</u> Growth

Forward P/E Ratio
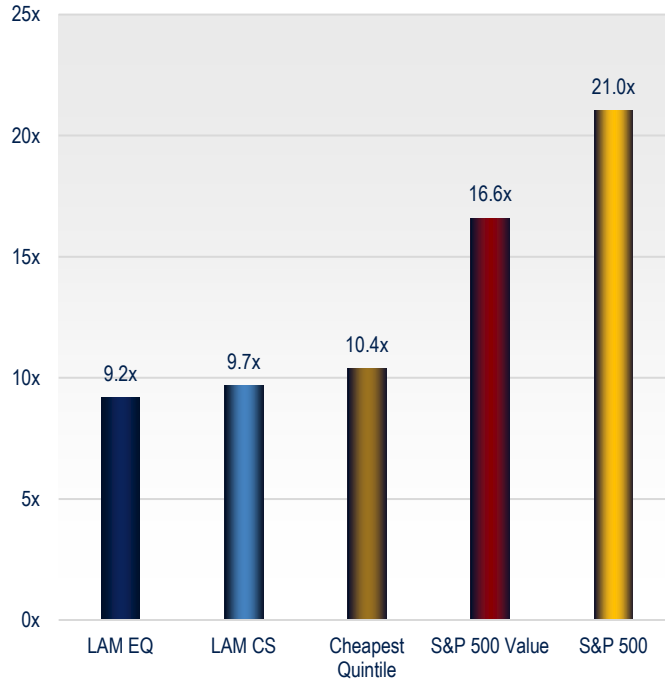
Category	P/E
LAM EQ	9.2x
LAM CS	9.7x
Cheapest Quintile	10.4x
S&P 500 Value	16.6x
S&P 500	21.0x

Indexed EPS Growth

LAM – CS: +6.5%
LAM – EQ: +6.1%
S&P 500: +4.5%
Cheapest Quintile: +2.5%
S&P 500 Value: +2.0%

X-axis: 2007 A, 2008 A, 2009 A, 2010 A, 2011 A, 2012 A, 2013 A, 2014 A, 2015 A, 2016 A, 2017 A, 2018 A, 2019 A, 2020 E, 2021 E

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Value
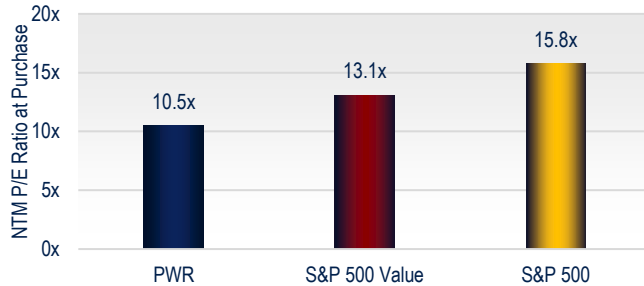
Quality

Analyzability
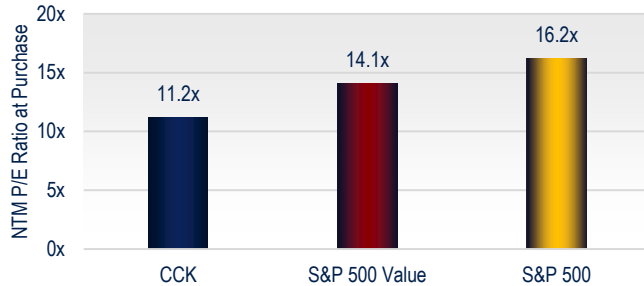

Business Background

- Provides specialty infrastructure services including maintenance work, emergency repairs, and new project construction
- Has the largest specialty workforce in North America and essentially is an outsourced contractor for many major utility and telecom companies
- Approximately 55% of sales are generated from Electric Power, 42% from Oil & Gas, and 3% from Telecom
- The base of its operations is comprised of maintenance type work that is recurring and inherently stable, and accounts for 80-85% of sales
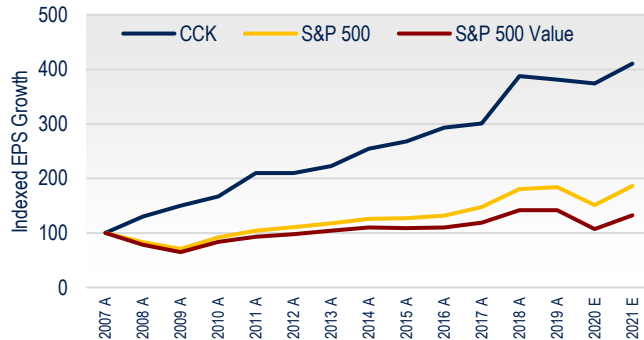
Current Trends

- Attractive 15% return on tangible capital
- Local knowledge, flexible cost structure, skilled employees, mostly pass-through pricing, repeatable revenue, and long-standing relationships all key elements making this a high-quality business
- Has a strong balance sheet (<1x Net Debt / EBITDA) and produces strong cash flow, enabling it to reduce its share count by 32% since 2014
- Telecom business has potential to more than double in size

Example Investment: Crown Holdings (CCK) – Purchased Apr 2018

Value

NTM P/E Ratio at Purchase

- CCK: 11.2x
- S&P 500 Value: 14.1x
- S&P 500: 16.2x

Quality

Indexed EPS Growth — CCK, S&P 500, S&P 500 Value (2007 A – 2021 E)

Analyzability

Business Background
- Second largest global producer of beverage and food cans
- Growth in can business is steady with limited economic sensitivity
- High-quality business with steady returns on tangible capital above 20%
- Plants benefit from dominant local market shares

Current Trends
- Cans benefit from secular shift in consumption as they are an increasingly preferred method of packaging
- Nearly 60% of beer volumes in the U.S. are now packaged in cans versus only 48% in 2006
- Stable margins as raw material inputs are passed through on customer contracts
- Company recently completed acquisition of Signode, a leader in transit packaging. The acquisition is materially accretive and provides new avenue for growth

Summary

- Value <u>indices</u> have struggled for over a decade

- However, value <u>stocks</u> performed well after GFC, but then struggled for ~2 years

- You can't get value stock performance from the value index

- Recent value stock performance is consistent with historical value cycles

- The next value upcycle has the potential to be one of the best

- Timing is tricky but upcycle may have started after March 18th

- Lyrical seeks to find the "gems" within the "junk"

Disclaimer

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MARKET DATA IS COURTESY OF FACTSET.

Important Notes

Index Information

The S&P 500 Index is a market capitalization weighted index comprised of 500 widely-held common stocks.

The S&P 5000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those S&P 500 companies with lower price-to-book ratios and lower expected growth values. The S&P 500 Value Index is constructed to provide a comprehensive and unbiased barometer of the large-cap value segment. The index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect value characteristics.

Returns by NTM P/E Quintiles (Slides 3 – 10, 14)

For each calendar quarter, based on FactSet data, we divided the 1,000 largest U.S. stocks by market capitalization into quintiles based on their beginning of quarter price to median forward earnings multiple. Return for each quintile is the simple average of the total returns, including dividends, of each stock in that quintile. Returns for stocks that ceased trading are included through the date they ceased trading. The universe average is the simple average total return of the 1,000 stocks over the period presented.

The returns reflected in the charts are annualized. This does not reflect the experience of any investor.

History of Value Performance Cycles (Slide 11-13)

For the period from January 1960 – December 1984 we use Sanford Bernstein data for the cheapest quintile within the 1,000 largest U.S. stocks by market capitalization based on price to book value as the representative cheapest quintile.

For the period from January 1985 – December 1997 for each quarter, based on FactSet data, we divided the 1,000 largest U.S. stocks by market capitalization into quintiles based on their beginning of quarter price to median *trailing* earnings multiple. Return for the lowest p/e quintile is the simple average of the total returns, including dividends, of each stock in that quintile. Returns for stocks that ceased trading are included through the date they ceased trading.

For all periods after 1997 we use the methodology described in the Notes to Slides 3-10 set forth above.

Note that discretion was applied by Lyrical in determining the beginning and ending of each cycle.