LRT CAPITAL MANAGEMENT

THE VISION TO SEE
UNREALIZED VALUE

June 1, 2021

May 2021 - Investor Update

Dear Friends & Partners,

Our investment returns are summarized in the table below:

Strategy	Month	YTD	12 Months	24 Months	Inception
LRT Economic Moat	+1.09%	+12.23%	+46.85%	+6.59%	+26.94%

Results as of 5/31/2021. Periods longer than one year are annualized. All results are net of all fees and expenses. Past returns are no guarantee of future results. Please contact us if you would like to receive a full performance tearsheet. Please see the end of this letter for additional disclosures.

During the month of May, the LRT Economic Moat strategy returned +1.09% net of fees.

In the LRT Economic Moat strategy, as of June 1st, 2021, our net exposure was 93.89% and our net beta-adjusted exposure was 56.01%. We currently have 38 long positions and our top 10 positions account for 56.34% of our total long exposure. We believe that we are very well positioned for an eventual market correction, which we are certain is coming at some point this year. The likely catalysts for this upcoming market decline are fears of higher interest rates and inflation, or the prospect of the U.S. Federal Reserve ending or simply curtailing its asset purchase program which began last year in response to the Covid-19 pandemic.

There has been considerable carnage in high-growth and high-valuations stocks over the past four months. For the first time in over a year we see opportunities to make incremental investments in new companies. A lot of the declines we have witnessed are justified as the companies in question had dubious long-term prospects (Fastly, Beyond Meat), despite their fast growth. However, amongst the wreckage lie opportunities, as there are high quality companies whose share prices are down while the fundamentals of their businesses are better than ever. Several interesting names have come onto our radar after being down 20%, 30% and even 40% off their highs. We don't believe that we have seen the worst of the sell-off in high growth companies yet but we are looking forward to acquiring shares in select companies if the broad market correction we expect in the second half of the year materializes. Stay tuned for more details on this front in the months ahead.

Finally, we would like to welcome Shugo Tanaka from UNC, and Jimmy Qian from UT, as our summer interns into the LRT Capital team. If you are interested in joining our team, please email careers@lrtcapital.com.

Back to Basics

It is important to periodically reiterate our investment philosophy. At LRT, we are exclusively focused on long-term investing in high-quality companies, which we believe will compound their intrinsic value at a rate higher than the overall stock market. We believe that exceptional investment results come not from stock market timing but from owning businesses with exceptional stock price returns over time. What's more, we believe that stock prices themselves follow business results over the long-term. Therefore, exceptional stock returns come from exceptional business returns on a **per-share** basis.

We are long-term investors and we do not try to dance in and out of the market. We are always fully invested. We believe it is futile to predict short-term market movements. In fact, we view stock market volatility as a source of opportunity because it allows us to occasionally purchase shares in exceptional companies at very attractive prices. Thereafter, we seek to hold our investments for as long as possible to allow the power of capital compounding to take effect. Because we seek to invest for the long-term and believe market timing is a futile attempt, we invest only in high-quality companies, i.e. those possessing sustainable competitive advantages (moats), the ability to grow and reinvest capital over time, and management that excels at capital allocation. If we are right about the trajectory of the businesses we invest in, over time, we will be right on the trajectory of their stock prices as well.

Random Thoughts About Incorrect Forecasts

Super Bowl XLIX, which was played in Arizona in early 2015 between the Seattle Seahawks and the New England Patriots, ended with a win by the Patriots after what has come to be one of the most controversial plays in Super Bowl history. To set the scene: New England was up by four points with 26 seconds left in the game, and Seattle had possession of the ball on the one-yard line on the 4th down. The expectations were that Seattle would attempt a running play to advance the required one yard, win the game and be crowned Super Bowl champions. Instead, Seattle attempted a passing play, and the pass ended up being intercepted – a terrible outcome that ended the Seahawks' dreams of winning the game.[1]

This decision, which ended up costing Seattle the Super Bowl, was universally criticized. Sports commentators considered the decision to go for a passing play instead of a run a huge blunder on the part of the coach Pete Carroll.[2] Critics couldn't decide if this was the single worst decision by a coach in Super Bowl history or all of NFL history. But was it really? Imagine what would have happened if the play was completed in the endzone and the Seahawks ended up winning the game. What would the newspaper headlines look like the next day? Would it still have been the worst decision ever? The Seattle Seahawks would have been Super Bowl champions and most commentators would probably say the pass play was a great call. In fact, we don't have to imagine anything, because in Super Bowl LII, between the Philadelphia Eagles and the New England Patriots (yes, again), a similar situation occurred at the end of the 2nd quarter. This time around, when the passing play was made and a touchdown scored, the same commentator, Cris Collinsworth was quite complementary.

Pete Carroll's decision to go for a passing play in Super Bowl XLIX was a good decision – despite all the negative commentary around it. It was a good decision because of the time constraints (26 seconds left in

[1] Credit for the original story goes to Annie Duke.

[2] "It's gotta be one of the dumbest calls offensively in Super Bowl history!" – Cris Collinsworth, sports commentator

the game). Since the running play was expected, the defense would have been prepared for it, making it harder to complete. If a running play was called and failed to gain the required one yard, the coach could call a time-out and attempt one more running play. But by going for a pass, which was not expected by the defense, there were three possible outcomes: touchdown (winning the game), incomplete (in which case the clock stops automatically without a time-out), or interception (which happens less than 2% of the time in these situations). If the passing play ended in a touchdown, the call would have most likely been hailed a "brilliant" decision, but if it was incomplete, a further two running plays could have been attempted. Since the odds of a touchdown in this case were many times higher than that of an interception, this was ultimately the right decision to make. Pete Carroll was simply unlucky.

Almost all outcomes in life contain an element of randomness or luck. Therefore, decisions must be judged based on the information that is available at the time of the decisions, and not the eventual outcome. Yet, when judging decisions, we often conflate the call itself with the eventual result. Judging decisions by their results is convenient, but incorrect. If you drive drunk and get home safely, was that a good decision? Most drunk drivers do not get into fatal accidents. Does that make drunk driving a good decision? Similarly, running a red light can often be consequence free. Does that mean running red lights is a good idea? In these examples it is easy to see what is right, but in most areas of life, the connection between decisions and outcomes is much more complex. We can all agree that drunk driving is a bad decision. Why then do most of us insist on evaluating decisions based on outcomes in so many other areas of life? If after careful consideration you hire a candidate for a job and they quit after three weeks, was that a bad decision? If a company launches a new product and it flops, was it a bad decision? If after careful research you buy a stock and it goes down, was that a bad decision? The mental shortcut of judging decisions by their results can lead us to some terrible lessons. When we equate the quality of the decision with the outcome, we are engaged in what is called "resulting". Are you a "resulter"?

Resulting makes it hard for us to draw the correct lessons from decisions. After Hillary Clinton's surprise loss to Donald Trump in the 2016 U.S. Presidential Election, many articles blamed her campaign for not putting more resources into Michigan, Wisconsin and Ohio while instead campaigning vigorously in Pennsylvania. The Clinton campaign was called arrogant, out-of-touch, and "taking voters for granted" by not campaigning in states that had previously been called part of the "Blue Wall".[3] This is a perfect illustration of "resulting". The truth is that there were no articles written prior to the election calling for Hillary to spend time and resources in Michigan. In fact, it was the Trump campaign that was widely criticized for campaigning in places where they already had overwhelming support.[4] All pre-election surveys showed Clinton with comfortable leads in Michigan, Wisconsin and Ohio, while Pennsylvania was closer to a toss-up. Was it not therefore rational for Hillary to campaign in the states where her presence could really change the election? Hillary Clinton ended up losing Michigan, Wisconsin, Ohio, **and Pennsylvania** – each by less than 1%.[5] The pre-election polls were clearly off by a lot. Was the decision to focus on Pennsylvania a bad one? Was Trump's decision to hold rallies in Alabama, a state that he would have almost certainly won without ever stepping foot in it, a sound strategy? Afterall, U.S. Presidential elections are decided by the electoral college, with each state being a winner-take-all simple majority contest.[6] A candidate who wins 50.1% of a state's votes gets the same amount of electoral college votes as

[3] https://www.theatlantic.com/politics/archive/2016/11/trumps-road-to-victory/507203/

[4] https://www.cnn.com/2015/08/21/politics/donald-trump-rally-mobile-alabama/index.html

[5] If you exercise and lose weight, but end up dying of a heart attack, was all the effort futile?

[6] Maine and Nebraska are exceptions to this rule. See: https://www.270towin.com/content/split-electoral-votes-maine-and-nebraska/

if he had won it by 90%. As a result, traditionally, U.S. Presidential political campaigns focus their efforts on a few select "swing states" while ignoring the majority of "deep red" and "deep blue" states. Was Trump a political genius or was he simply lucky? Luck clearly plays a role in life. Without it, how would we explain the success of those we do not like?

I remember an event many years ago where I met an investor who had recently purchased shares in Microsoft (MSFT). At the time the core of his investment thesis was the opportunity for the company to catch up in the mobile market. Windows Mobile had a tiny market share compared to Apple's iOS and Google's Android, but the investor in question believed the company could gain share. He described a complicated process by which the company would pay developers of key apps to port them to the Windows Mobile OS to increase the appeal of the system to users and how over time they would gain share with device makers. Since then, Microsoft stock has done very well indeed, but not because of anything to do with Windows Mobile[7], but rather the rise of cloud computing, the company's Azure division, and the firm's successful transition to a subscription-based software sales model. Curiously, the investor I spoke to was entirely focused on the mobile market and didn't even mention cloud computing. Was the investor's decision to buy Microsoft shares a good decision? What lesson did he learn from the outcome of his investment? Does he even remember the original investment thesis for buying the stock, which turned out to be completely wrong? Does he acknowledge that he simply got lucky? The truth is we will never know.

This is what makes investing such a difficult endeavor. Investing is a wicked learning environment[8]: the feedback is noisy, the outcomes heavily influenced by randomness, the timing of the results is often inconsistent. The world does not provide us with clear information that enables us to improve our decision making. It presents us with messy data that is incomplete, unrepresentative, ambiguous, inconsistent, and often random. As investors trying to discern patterns we are often groping in the dark. The world is far too complex to be completely understood, and the environment is constantly changing. As a result, our understanding is always imperfect and our search for answers full of mental shortcuts, analogies, and simplifications. When trying to understand the world, we are often like a black man, in a black room (with no lights), whose dimensions we don't know, trying to find a black hat that may not even be there in the first place. Or to paraphrase it another way: "Most haystacks don't even have a needle."[9]

Learning from data is hard, not only because the data is noisy, but also because our own minds are biased by our preexisting beliefs and our ability to find patterns that match our beliefs – whether they are true or not. For example, when studying cancer rates in the United States, one can find a remarkable pattern: the highest prevalence of kidney cancer is in small rural counties that overwhelmingly vote Republican in U.S. Presidential elections.[10] If you are inclined to support the political left in the United States, your mind will immediately come up with reasons for this: poor access to healthcare due to Republican policies, lax pollution standards, or bad dietary habits. Now imagine if I told you the opposite was true: the lowest kidney cancer rates are found in small rural counties that overwhelmingly vote Republican in U.S. Presidential elections. If you like rural America, your mind will also find explanations for these low cancer rates: a healthier rural lifestyle, a diet based on food closer to where it was produced, plenty of fresh air, etc. This pattern of thinking is called motivated reasoning – your mind is working hard to summon evidence that supports your beliefs. The reality is that both statements are true, both the highest rates of kidney cancer

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[7] https://www.theverge.com/2017/10/9/16446280/microsoft-finally-admits-windows-phone-is-dead

[8] https://www.psychologytoday.com/us/blog/experience-studio/202007/experience-kind-vs-wicked

[9] Credit to @LibertyRPF, https://twitter.com/LibertyRPF

[10] https://statecancerprofiles.cancer.gov/ ; https://www.usnews.com/news/healthiest-communities/slideshows/counties-with-the-highest-cancer-rates-in-the-us

and the lowest rates of kidney cancer are found in U.S. counties that favor Republicans in the Presidential elections. How can this be? The key lies in the fact that they are **small counties** and sampling from a smaller population is always more likely to lead to extreme outcomes purely based on luck. Political affiliation does not play a role in cancer risk.

What do small sample sizes, and extreme outcomes have to do with investing, you might ask? A finding in the data showing high cancer rates in Republican counties will often be highly publicized, if the reporter or researcher in question has a political leaning that supports a conclusion in-line with their political beliefs.[11,12] But if the beliefs do not align with the data, the finding is unlikely to generate much interest. This is analogous to investing, in that more extreme outcomes are more likely to garner media attention. How do extreme outcomes occur in investing? Through concentration. Concentrated investing is unduly praised by allocators and investment commentators alike. Concentrated investing is often applauded as "investing with conviction", but investment conviction only matters if it is aligned with your ability to be correct. There are no points in investing for having strong convictions that turn out to be totally wrong. Having strong convictions and being **wrong** is a path towards disaster. The problem is that concentrated investing leads to extreme outcomes, but it is mainly the successful outcomes that are seen by allocators and stock market journalists. Simply put, funds that have a concentrated strategy but fail to perform <u>are not marketed</u>. So when you see a pitch deck from a fund with a great track record that hails investment concentration as a path towards success, ask yourself how much of what you are seeing is simply luck and how predictable the past success is of future returns. One ultra-concentrated manager is Bruce Berkowitz from Fairholme Funds who was named Morningstar's "Domestic Equity Fund Manager of the Decade (2000-2009)". He clearly had "conviction", yet over the next seven years he lost 89%.[13]

Concentrated portfolios are good for generating headlines, but **consistent performance** is a function of risk management, careful portfolio construction and a repeatable investment process. At LRT we divide our investment process into two clearly differentiated parts: 1) a discretionary and **qualitative** selection of investment ideas, and 2) a **quantitative** and rules-based portfolio construction. In the investment community, a lot of time and ink is spilled over the first part of this process: finding good investment ideas. This is reflected in all of the stock-pitch competitions you hear about and the focus on one's "best ideas". But we believe it is the second part of the investment process, the portfolio construction that is often overlooked and where managers can add great value. A systematic and quantitative process for portfolio construction, risk management and rebalancing are what leads to more consistent performance over time.

At LRT, our portfolio position sizing is a function of inverse variance, which means that the riskier a position, the smaller it is in the portfolio. Our portfolio construction process also considers the correlation between the positions, with portfolio holdings that bring more idiosyncratic (stock specific) risk being given a higher weighting. Finally, we rebalance our portfolio mechanistically, every month, trimming stocks that outperform, and adding to those that underperform. Taken together, we believe, this systematic approach to portfolio construction and risk management helps us produce more consistent investment performance while minimizing the risks of a large drawdown. We look forward to answering any questions you might have about our investment process and portfolio construction in particular.

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[11] https://www.sciencedaily.com/releases/2018/09/180905083932.htm

[12] https://www.ncbi.nlm.nih.gov/pmc/articles/PMC4692249/

[13] https://www.financialexpress.com/market/decades-former-best-fund-manager-loses-83-wealth-on-a-small-mistake/746464/ ; Even after a huge recent rally, Fairholme Fund (FAIRX) 10-year CAGR is 0.34%, compared to 14.29% for the S&P 500 over the same time period.

Our Portfolio

The top ten investments in our portfolio as of 6/1/2021, in order of position size, are presented on the following pages. All valuation metrics and returns are as of 6/1/2021 unless otherwise stated. For a relative valuation context, the S&P500 is currently trading at 37.24x trailing and 22.55x forward earnings, respectively – one of the highest valuations ever recorded.[14] The Russell 2000 trades at a forward PE ratio of over 31.91x – also an extremely high number. We believe our portfolio will generate far superior returns than the S&P500 going forward.

The table below gives additional insight into our portfolio exposure. We are dramatically underexposed in technology, communication, and financial services, while being overexposed in consumer cyclicals, consumer defensives and industrials. These sector weightings are an outcome of where we currently see opportunities, and not a top down decision based on macro predictions. We will happily own many technology companies if their valuations become more attractive.

Portfolio Statistics *as of 6/1/2021*[15]			
Sector Allocations (Long Exposure, %)			
S&P 500 Sector	**Portfolio**	**S&P 500**	**Delta**
Consumer Cyclical	21.91	12.44	9.47
Industrials	21.63	9.06	12.57
Consumer Defensive	16.62	6.4	10.22
Healthcare	10.96	12.9	-1.94
Basic Materials	6.93	2.34	4.59
Communication Services	4.42	11.18	-6.76
Energy	4.45	2.67	1.78
Real Estate	5.17	2.53	2.64
Financial Services	5.59	14.4	-8.81
Technology	2.32	23.46	-21.14
Utilities	0	2.62	-2.62
Market Cap Allocations (%)			
Large			24.89
Mid			54.47
Small			20.64
Country Allocations (%)			
United States			84.53
Canada			9.31
Denmark			5.11
Singapore			1.05

[14] https://www.wsj.com/market-data/stocks/peyields

[15] Source: Bloomberg, Morningstar, Sentieo.

#1 - The Clorox Company (CLX)

For several months now, our largest position has been Clorox – the cleaning products company. Besides wipes, the company also manufactures bleach, charcoal, cat litter, plastic bags, and container products. Clorox benefited during the Covid-19 pandemic from an increased demand for cleaning products. Companies and consumers trust the Clorox brand – a source of the company's huge competitive advantage. United Airlines, for example, chose to partner with Clorox in its push to reassure consumers about the safety of air travel.

Clorox reports business results in four segments:

Segment	Share of revenue[16]
Health and Wellness (Cleaning; Professional Products; Vitamins, Minerals and Supplements)	41.70%
Household (Bags and Wraps, Grilling, Cat Litter)	25.65%
Lifestyle (Food, Water Filtration, Natural Personal Care)	16.75%
International (Sales Outside the U.S.)	15.89%

Clorox is a typical "defensive" holding – subject to very small fluctuations in end market demand. The whipsaw in demand that the company is currently going through due to Covid-19 pandemic is unique in the company's history. While down from record levels in Q1 2020, its branded consumer products remain in strong demand. Historically (before Covid-19), the company's sales grew in line with GDP, while earnings-per-share grew slightly faster due to operational and financial leverage. We expect sales will decline slightly in the next few quarters as the Covid-19 pandemic comes to an end, but we believe this decline is more than accounted for by the company's low valuation.

There was very little to like in Clorox's latest earnings report. Organic sales growth was -1% vs and +3.1% consensus. Revenue was flat year-over-year, and while earnings per share beat analyst estimates, they were down 14% from the prior year quarter. On top of all of that, the company downgraded its annual outlook due to rising input costs (the company mentioned "inflation" eight times during the earnings conference calls) and freight costs.[17] Of course, Clorox is now lapping H1 of 2020, a very unusual period, when the company's sales exploded due to the Covid-19 pandemic. Despite the company's challenging comps, Clorox has guided to top line growth of 10-13%, and EPS growth of +1-4%. While the results were disappointing, they appear entirely due to the demand fluctuations caused by the improvements in the Covid-19 situation. We don't believe it makes sense to read too much into one quarter of the company's performance especially given the whipsawing of end market demand due to Covid-19. We see the company's competitive position as strong and their brands as more relevant than ever.

Shares are -11.5% year-to-date and -11.93% over the past twelve months.

[16] Source: Clorox, 8-K Earnings, Update, 30-Apr-21

[17] The Clorox Company, Q3 2021 Earnings Call, Apr 30, 2021

#2 - Domino's Pizza, Inc. (DPZ)

Domino’s Pizza is the world’s largest franchisor of pizza restaurants with over 13,800 locations in 85 countries. As for any restaurant operator, the key metric to consider for Domino’s Pizza is same-store-sales (SSS) growth. Growing same-store-sales are ultimately how a restaurant business increases earnings from its existing assets. On this criterion the company continues to impress, with SSS having grown in the U.S. for 40 consecutive quarters, and an astounding 109 straight quarters internationally.

Two-thirds of the company’s stores are currently abroad, and the international segment remains the company’s largest growth opportunity, as the penetration of convenient fast food remains lower abroad than in the United States. Pizza is a product with exceptionally high gross margins, one that “translates” well across different cultures, and one that literally “travels well”, not losing much of its appeal when delivered in a cardboard box. The rise of 3rd party delivery platforms such as Uber Eats, Doordash and Grubhub is challenging the pizza category as it has expanded the number of choices consumers have for convenient takeout. However, the economics of food delivery remain challenging for most restaurants and platforms alike[18], while pizza delivery continues to be highly profitable. Regardless of how the “delivery wars” currently playing out end, Domino’s financial results show little impact of this increased competition, and the company continues to deliver exceptional financial performance.

Domino’s Pizza stock is not optically cheap at 29x forward earnings, however, the company has routinely reported earnings growth of over 20% in almost all quarters since 2009. Given the company’s high growth rate, international growth opportunities, and capital light business model, which allows for returns on invested capital of over 40%, we are happy to continue to hold the shares.

In late April, Domino's Pizza reported Q1 2021 earnings. Comparable sales in the U.S. were +13.4% beating expectation for a rise of +9.7%; Company-operated stores saw comparable sales increase +6.3% during the quarter, while franchised outlets saw a gain of +13.9%. International stores saw comparable sales increase +11.8% vs +6.0% consensus. Operating margin reported was 19.0% of sales vs. 18.2% consensus. While net income was down 3.2% from a year ago, this was driven by a change in the company’s tax rate, rather than poor business performance.[19] The company added 175 net new stores to its system during the quarter (36 US, 139 International). Domino’s Pizza continues to aggressively repurchase its shares and currently has an active $1 billion repurchase plan in place.

Shares are +11.61% year-to-date and +17.79% over the past twelve months.

[18] DoorDash lost $312 million in Q4, 2020. Source: DoorDash, 8-K Earnings, Update, 25-Feb-21

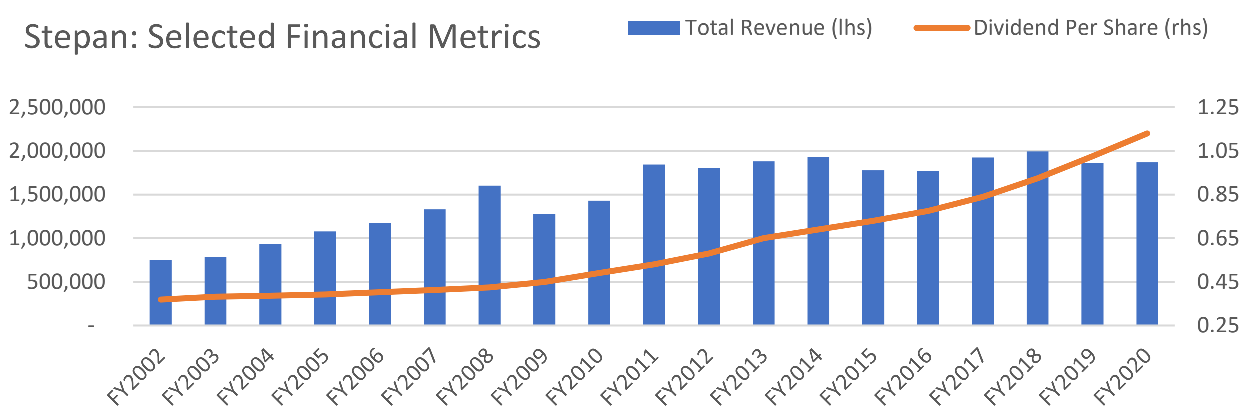
[19] Source: Domino’s Pizza, 8-K Earnings, 29-Apr-21

#3 - Stepan Company (SCL)

Stepan is an under-the-radar company with a market capitalization of approximately $3.0b.[20] The company is engaged in the manufacturing of specialty chemicals, primarily for the cleaning industry. The company's products are the principal ingredients in consumer and industrial cleaning products such as washing detergents, as well as shampoos, body washes, and fabric softeners. The company's specialty products include emulsifiers, food stabilizers, flavorings, and nutritional supplements.

Segment	Share of revenue[21]
Surfactants	68.98%
Polymers	27.97%
Specialty Products	3.05%

Don't let the dullness of the company's products fool you. While Stepan operates in a commoditized industry, the company has been an efficient operator and has been able to expand margins over time. What looks on the surface like a cyclical, commoditized business is in fact a very resilient provider of key inputs to daily necessities such as body and household cleaning products. Due to its resilience through different economic cycles, Stepan has been able to increase its annual dividend for 54 years in a row. What's more, payouts to shareholders did not come at the expense of reinvesting in the business. The company has grown earnings-per-share by a factor of 5x over the last two decades while maintaining returns on invested capital in the mid-teens.



Stepan reported excellent results for the first calendar quarter of 2021. Revenue was +19.5% year-over-year, net income was up +47%, and adjusted EPS +75%. The company beat estimates on both the top and bottom line. Revenue growth was driven primarily by higher prices +13%, followed by volume +6%. The company's management was very up-beat during the conference call citing very strong customer demand.[22]

Shares are +13.4% year-to-date and +37.16% over the past twelve months.

[20] As of 5/1/2021. Source: Sentieo.

[21] Source: Stepan, 8-K Earnings, 27-Apr-21

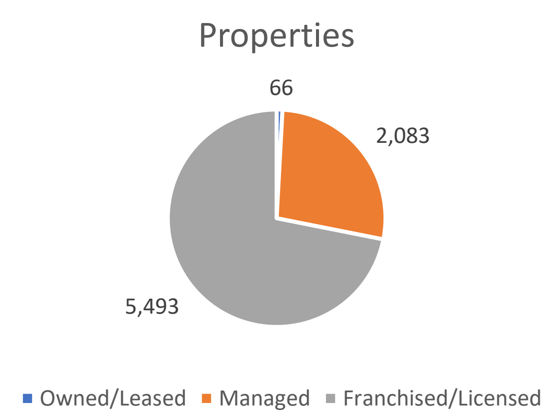
[22] SCL Stepan Company, Q1 2021 Earnings Call, Apr 27, 2021

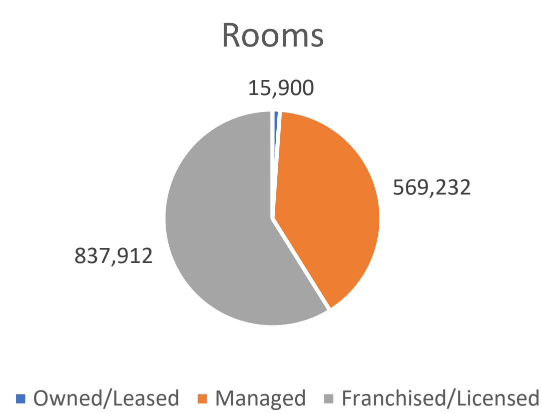
#4 - Marriott International, Inc. (MAR)

Marriott is the world's largest hotel company followed closely by Hilton (HLT) and Intercontinental Hotels Group plc (IHG). The company owns a portfolio of brands from the low end (Courtyard, SpringHill Suites, Aloft), through the mid-tier (Marriott, Sheraton, Westin, Renaissance Hotels), to the luxury high end (JW Marriot, Ritz-Carlton, St. Regis). In total the company had 7,642 properties with over 1.4 million rooms as of the end of Q1 2021.[23]

The majority (85%) of Marriott's revenue comes from hotels in the United States, with the rest almost evenly split between Asia Pacific and Europe. Like it's smaller peer, Hilton, the company today is almost exclusively a manager and franchisor of hotels, not a hotel owner. The company owns 66 hotels, manages 2,083 and franchises 5,493. Like all franchise-based businesses Marriott requires very little capital to grow as it utilizes the investment capital of its hotel-owners/partners to expand. Marriott currently faces a difficult operating environment due to the Covid-19 pandemic and uncertainty about the future of business travel. However, the company is an excellent operator with a somewhat leveraged capital structure (the company acquired Starwood Properties in late 2016) – if pent-up demand for travel materializes post-Covid, as we expect it will, the company will quickly go from losing money to raking in profits.

We are also long shares of Hilton Worldwide Holdings Inc. (HLT). Our investment thesis with respect to Hilton is essentially the same as with Marriott: excellent business economics, a consolidating industry, and a good track record of capital allocation. If our HLT shares were added to our MAR shares, together they would still be our 4th largest position in the portfolio. Shares of Hilton are +12.59% year-to-date and +55.38% over the past twelve months.





Last earnings report: May 10th, 2021

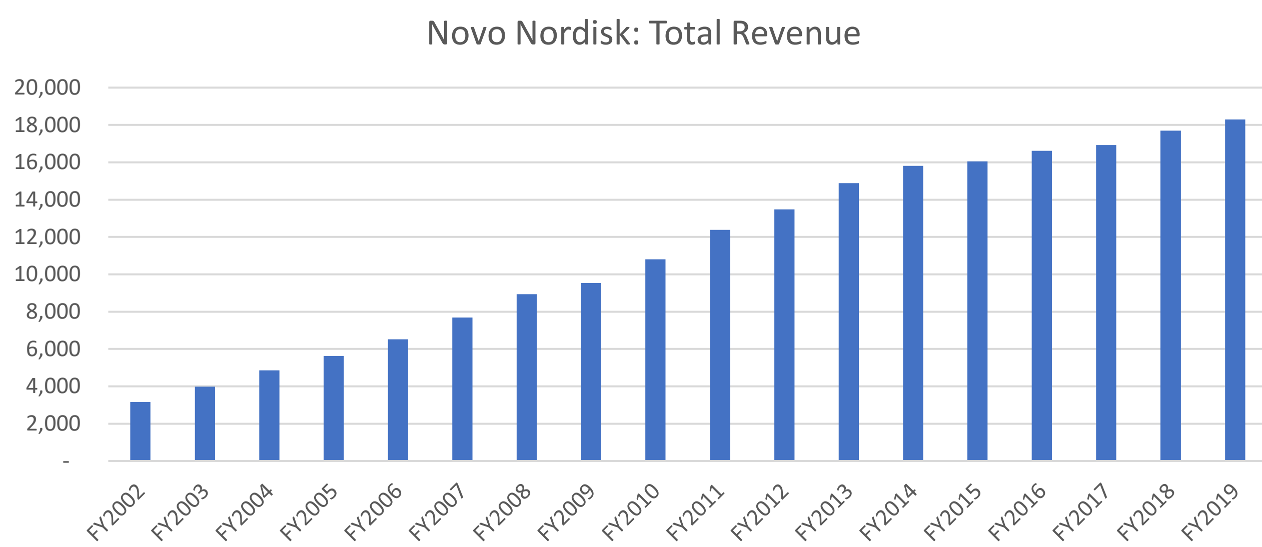
Shares are +8.84% year-to-date and +56.68% over the past twelve months.

[23] Source: Marriott, 10-K/A, 02-Apr-21

#5 - Novo Nordisk A/S (NVO)

Novo Nordisk is the global leader in insulin, which is, sadly, a growing business as more and more people around the world suffer from diabetes. Millions of people need daily injections of insulin to stay alive[24], a number that, unfortunately, is likely to continue to grow by millions more in the coming decade. It may seem at first glance that insulin should be a commoditized business, after all, it was discovered and synthesized over a hundred years ago, but nothing could be further from the truth. There are many types of insulin and Novo Nordisk has spent billions on R&D over the years to develop new products. On February 11th, the company reported favorable results from a phase-3 trial of Semaglutide, a drug that is currently used for Type 2 diabetes treatment. The study evaluated the use of Semaglutide for weight loss treatment in non-diabetic patients and found a significant impact on weight loss for patients receiving Semaglutide vs. the placebo control group. If Semaglutide is approved for weight loss treatment, we expect it will be meaningfully accretive to the company's bottom line.

The company's proprietary product line supports returns on invested capital of over 40%, and while sales growth is relatively slow (+6% annualized CAGR over the past decade), the company's shares trade at a reasonable valuation of only 22x forward earnings. For a company with an extremely predictable business, high returns on capital, and an easily forecastable future, we believe this to be highly attractive.



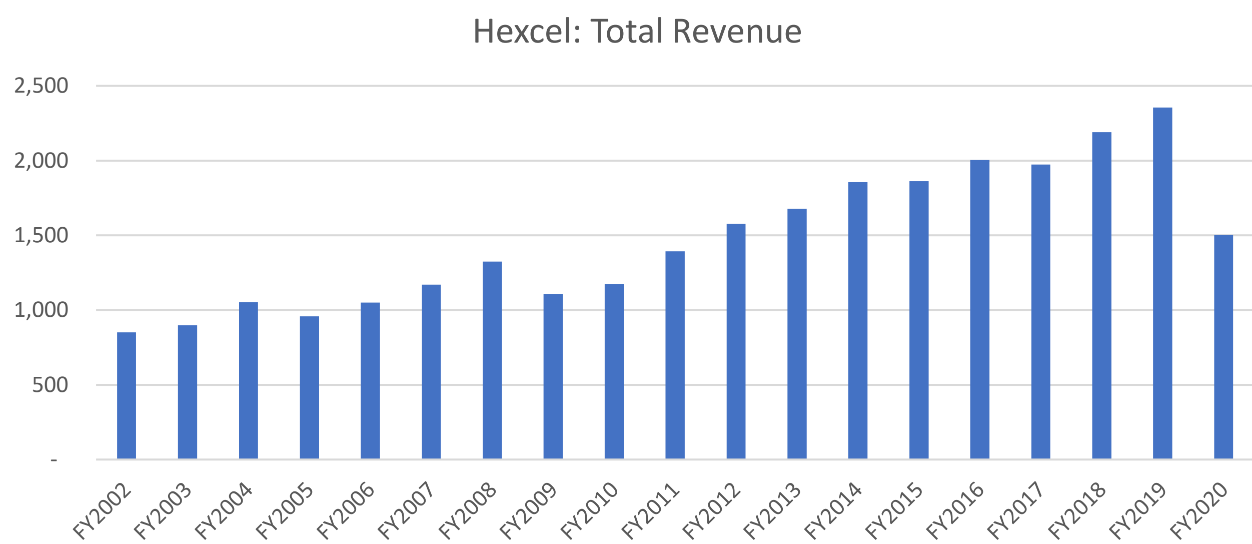
Shares are +14.57% year-to-date and +24.15% over the past twelve months.

[24] According to the WHO there are 422 million diabetics worldwide. This is estimated to increase to over 570 million by 2030.

#6 - Hexcel Corp. (HXL)

Hexcel manufactures carbon fiber composite materials with the primary end markets being aerospace and defense. The company's stock price was hit heavily last year due to the decline in the aerospace market, but the stock is making an impressive comeback this year as the outlook for travel and aerospace demand improves. The near-term demand for lightweight, high-performance carbon fiber composites is still uncertain, but the longer-term trend is clearly very strong. As airplane manufacturers look to improve the fuel efficiency and performance of their planes, the primary way of doing this is to reduce weight. The 787, 777X and A350 are just the most recent examples of planes from Boeing and Airbus that utilize an increasing amount of carbon fiber materials in their construction.

Segment	Share of revenue
Commercial Aerospace	47.60%
Space & Defense	36.00%
Industrial	16.40%



Hexcel reported a loss of $0.17 per share for Q1 2021, while revenue declined 43% year-over-year.[25] Just as is the case with Marriott, we do not view these results as meaningful or indicative of a long-term trend, but rather a once in a century aberration due to the Covid-19 pandemic. Once Covid-19 recedes, we expect the demand for more fuel-efficient planes to return rather quickly, powering the demand for the company's light weight carbon composites.

Shares are +22.62% year-to-date and +67.07% over the past twelve months.

[25] Source: Hexcel, 8-K Earnings, Update, Other, 19-Apr-21

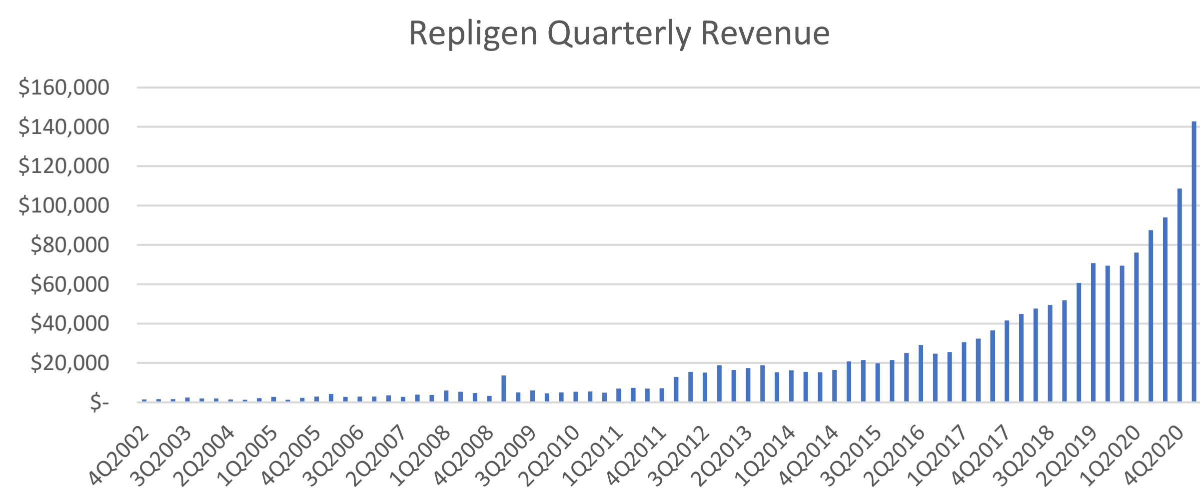
#7 - Repligen Corporation (RGEN)

Based in Waltham, MA, Repligen makes equipment for the biologic drug manufacturing industry. The company's main products are focus on filtration (48% of revenue), chromatography[26] (20% of revenue), process analytics products (9% of revenue), as well as select proteins used in the manufacturing of biological drugs (22%). We believe that biological drugs represent the most exciting frontier of medicine today, with monoclonal antibodies and gene therapy amongst the most promising approaches to tackling rare diseases.

The manufacturing of biological drugs is very different than that of traditional, "small molecule" drugs. Whereas the construction of a traditional line for a traditional small molecule drug might cost as little as $5 million dollars, the development and scaling of a biological manufacturing line can cost well over $100 million. Every biological manufacturing process is different, but their common feature is that the active ingredient in the drug is created by living cells and usually consists of a complex protein that is administered to the patient by injection. In the most general of terms the manufacturing of a biological drugs has the following stages:

- Creation and selection of cell culture to produce desired protein.
- Growth and amplification of selected cells – usually in a bioreactor.
- Filtration, purification, and isolation of active ingredient.
- Testing, quality assurance and packaging.

Under CEO Tony Hunt, Repligen has successfully reoriented itself away from selling commoditized inputs to the biological manufacturing process, towards selling specialized proprietary equipment – largely accomplished through M&A. Revenue grew at a CAGR of 22% before Tony joined the company and at 41% since then. Importantly, this growth has not come at the expense of margins of ROIC, which have remained very strong throughout the period.



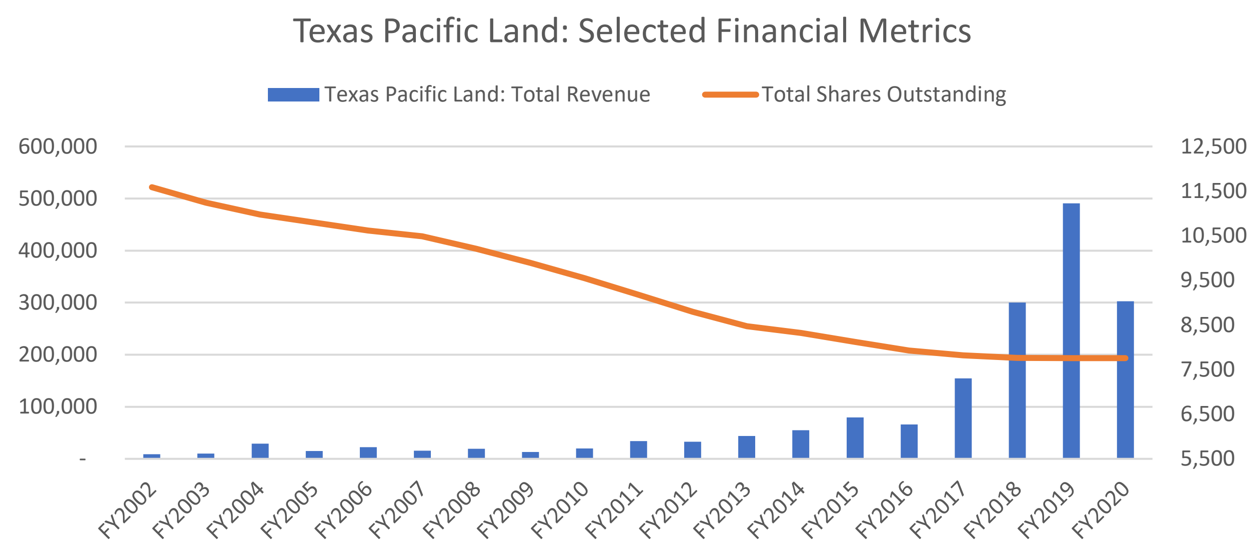
Shares are -4.71% year-to-date and +41.33% over the past twelve months.

26 https://www.nist.gov/video/what-chromatography-all-about

#8 - Texas Pacific Land Trust (TPL)

Long time readers will know that we rarely invest in commodity businesses. However, there are periods in the market where commodity-based businesses outperform the broad indexes by a wide margin. Therefore, in order to have balance in the portfolio, we have long searched for a competitively advantaged company in the commodity space. We believe that Texas Pacific Land Trust (TPL), meets that criteria. Formed out of assets of formerly bankrupt railroads, TPL controls the largest acreage of land in the Permian basin – the center of the US shale oil industry. The company has two main sources of income: 1) royalties from oil & gas extracted on its properties – essentially a free call option on future oil prices and production; and 2) a water business which develops water resources and sells services to the fracking industry. We see TPL as an effective way to diversify the portfolio into a commodity exposed business that has a history of smart capital allocation and low risk of financial distress during periods of low oil prices. The company has no debt, and $281 million in cash.[27]

The company uses most of its cash flows to pay dividends and repurchase shares.



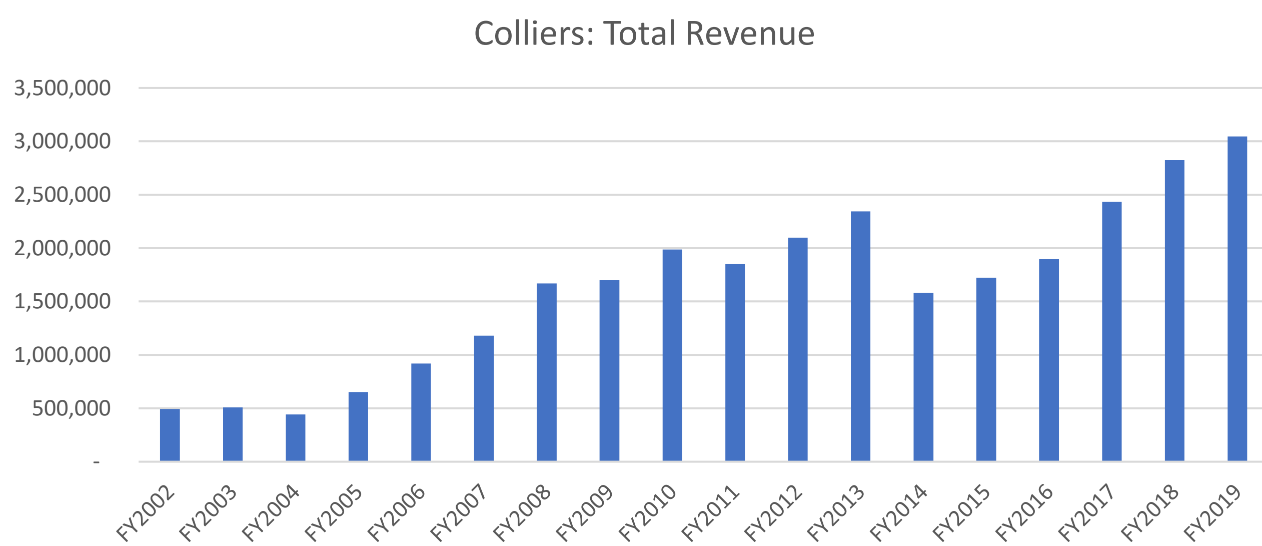
Shares are +100.35% year-to-date and +145.96% over the past twelve months.

[27] Source: TPL, Investor Presentation March 2021, 02-Mar-21

#9 - Colliers International Group Inc. (CIGI)

Colliers International Group is a commercial real estate brokerage and investment management company founded by Jay S. Hennick in 1976 in Toronto, Canada. From humble beginnings the company has grown, primarily through acquisitions, to become one of the five largest commercial real estate brokerages in the world (the others being CBRE, Jones Lang LaSalle, Cushman & Wakefield, and Savills). The company today offers a full range of services and reports in the following segments: Outsourcing & Advisory (45% of revenue; this includes Engineering & Design services, Valuation services and Property Management), Capital Markets (25% of revenue), Commercial Real Estate Leasing (24% of revenue), and Investment Management (6% of revenue). The company believes that about half of its revenue is recurring in nature. The Investment Management segment deserves special attention, as it is the result of an acquisition of the real estate investment management company Harrison Street in 2018. While the segment contributes the smallest part of revenues, it has a very high margin, contributing over 17% of the company's EBITDA.

Colliers has historically grown by acquisition and we expect it to continue to do so. The real estate services market is highly fragmented outside of North America presenting ample opportunities for Colliers to continue its growth strategy. The company has been a good steward of shareholder capital and spun out FirstService Residential (FSV) in 2014 to maximize the value of that business. This spin-out accounts for the drop in revenue in 2014 seen in the chart below.



Shares are +24.53% year-to-date and +111.76% over the past twelve months.

#10 - TFI International Inc. (TFII)

TFII International (formerly known as Transforce) is a recent addition to our portfolio – it is a Canadian logistics company with exceptional management operating in a consolidating industry. TFII came to our attention when they announced their purchase of the US operations of UPS Freight on January 25th, 2021. The company has a long history of growth through acquisition. Long time CEO Alain Bedard is fond of telling investors that he would rather own Scotiabank and get a 3% dividend than make deals that result in 3% returns[28]. This Canadian company also recently dual-listed in the United States.

UPS Freight, recently acquired by TFII, is a less-than-truckload (LTL) operation. LTL operations can build scale-based cost advantages as they require the consolidation of shipments in local hubs. This lends LTL operators to develop competitive moats based on local network density creating barriers to entry, as opposed to pure long-term trucking which is open to competition from anyone able to lease a truck. Pure play LTL companies such as SAIA, Inc. (SAIA) and Old Dominion Freight Line (ODFL) have historically generated very attractive returns for shareholders. Prior to the announced acquisition TFI already generated excellent returns for shareholders through very efficient operations and good capital allocation. Through the acquisition of UPS Freight US, the company immediately became one of the largest players in the US LTL market. The relatively low price paid for the asset (5.3x EBITDA pre-synergies, and the fact that UPS is taking a $500 million accounting charge on the deal) suggests TFII got a good deal. ODFL and SAIA both trade at over 15x EV/EBITDA.

We expect earnings to rise sharply at TFII over the next twelve months as the economy accelerates post-Covid. We are currently also long shares of Saia, Inc. (SAIA), the LTL operator headquartered in Georgia, based on the same investment thesis. If our SAIA shares were added to our TFII shares, together they would be our 5th largest position in the portfolio. Shares of Saia, Inc., are up +27.3% year-to-date and +110.08% over the past twelve months.

Shares are +86.48% year-to-date and +217.22% over the past twelve months.

[28] TFII Q2 2019 conference call.

<u>Other notable portfolio changes made during May:</u>

- **Target Corp. (TGT)** – reduce position, falling out of top ten.
- **A.O. Smith Corp. (AOS)** – reduce position, falling out of top ten.
- **Repligen Corporation (RGEN)** – new position established.

As always, I look forward to hearing from you and answering any questions you might have. Thank you for your continued interest and support.

Lukasz Tomicki
Portfolio Manager
LRT Capital

Appendix I: Attributions and Holdings as of 5/3/2021

LRT Economic Moat		Portfolio Statistics			
Top Holdings (%)		*Sector Allocations (Long Exposure)*			
The Clorox Company (CLX)	9.39	**Sector**	**Portfolio**	**S&P 500**	**Delta**
Stepan Company (SCL)	6.87	Industrials	24.28	9.22	15.06
Domino's Pizza, Inc. (DPZ)	6.64	Consumer Cyclical	21.50	12.21	9.29
Novo Nordisk A/S (NVO)	5.74	Consumer Defensive	17.34	6.59	10.75
Marriott International, Inc. (MAR)	5.55	Healthcare	8.81	13.13	-4.32
Hexcel Corp. (HXL)	4.80	Basic Materials	6.87	2.34	4.53
Texas Pacific Land Trust (TPL)	4.42	Communication Services	5.15	10.93	-5.78
Colliers International Group Inc. (CIGI)	3.73	Energy	4.43	2.79	1.64
AO Smith Corp. (AOS)	3.50	Real Estate	4.38	2.47	1.91
Target Corp. (TGT)	3.45	Financial Services	4.38	14.18	-9.8
Top Holdings Total	**54.10**	Technology	2.86	23.50	-20.64
		Utilities	0.00	2.65	-2.65
Hedges (%)		*Market Cap Allocations (%)*			
SPDR S&P MidCap 400 ETF (MDY)	-13.49	Large			26.06
iShares Core S&P Mid-Cap (IJH)	-13.49	Mid			53.60
iShares Russell 2000 (IWM)	-13.12	Small			21.79
iShares Core S&P Small-Cap (IJR)	-12.67				
Return Attribution (%)		*Country Allocations (%)*			
Long Equity	1.09	United States			80.46
Hedges	-0.38	Canada			12.76
Unlevered Gross Return	0.70	Denmark			5.47
Leveraged Gross Return	1.41	Singapore			1.30
Net Return	**1.09**				

Source: Morningstar, Sentieo.

Net returns are net of a hypothetical 1% annual management fee (charged quarterly) and 20% annual performance fee. Individual account results may vary due to the timing of investments and fee structure. Please consult your statements for exact results. Please see the end of this letter for additional disclosures.

Appendix II: Investment Philosophy

Over the past 36 months, we saw a large increase in the number of LRT Capital partners (the term we use to describe our clients). With so many newcomers, it is important that we write about our investment philosophy again.

Here are the key points:

- Exceptional stock returns come from exceptional business returns on a **per-share** basis.
- We seek to invest in high-quality companies, i.e. those possessing sustainable competitive advantages (moats), the ability to grow and reinvest capital over time, and management that excels at capital allocation.
- We only purchase companies whose shares trade at a discount to our assessment of their intrinsic value.
- It is futile to predict short-term market movements. We seek to hold our investments for as long as possible.
- The financial markets are dominated by short-term traders who see stocks as casino chips. This occasionally allows us to purchase shares in great companies at large discounts to their true worth.
- If we are right about the trajectory of the businesses we invest in, over time, we will be right on the trajectory of their stock prices.

We view stock market volatility as a source of opportunity. Volatility allows us to profit by acquiring shares in superb businesses at attractive prices. The more that markets (the "other" participants) are irrational, the more likely we are to reach our ambitious performance objectives.

In the long run, stocks are the best investment asset class, but our experience has taught us that our investment process will not generate linear returns. In some years, our portfolio will outperform, and in others, it will generate a below average return. This is a certainty that we must accept. We are long-term investors and we do not try to dance in and out of the market.

In summary, our investment strategy can be summed up in three steps:

- Only seek out high-quality companies.
- Do not overpay.
- Do nothing – patience and discipline are the keystones to success.

Disclaimer and Contact Information

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