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HS MANAGEMENT PARTNERS, LLC

# Second Quarter 2021 Investment Perspective

*investment styles ebb and flow . . . fundamentals never go out of favor*

July 12, 2021

## Investment Perspective

The big story of the second quarter was the cooling down of the U.S. 10-Year Treasury Yield. Rates had been on the rise since bottoming out last summer and had advanced further as 2021 began. This made sense. Aggressive monetary stimulus was being joined by large fiscal stimulus, and growing vaccination rates led to a reopening of the economy. Talk of rising prices, wages, and inflation was once again in the air.


*Source: Used with permission of Strategas Research Partners as of 7/1/2021. The 10s refer to ten-year treasury yields and 2s refer to two-year treasury yields.*

For now, it appears that Fed Chairman Powell has convinced the market that inflationary pressures are likely transitory. It seems the Fed's willingness to start "talking about talking about" reducing monetary stimulus has also created a sense of more vigilance regarding a response to inflation, if required. More than $12 trillion of negative yielding global debt in the market also certainly played a role in dampening the U.S. Treasury yield advance as well.

From our perspective, the rise that we had seen in the 10-year Treasury Bond Yield and the markets growing narrative toward cyclical recovery and reopening created an opportunity. Many high-quality growth stocks — including many that benefitted from the initial stay-at-home trade and the acceleration of several long-term trends — have seen their shares tread water or drift lower since last summer.

Narratives are always part of the market equation, sentiment and psychology. There is the stay-at-home versus reopening narrative highlighted above. There is the Growth versus Value narrative. There is the large cap versus small cap narrative. The list of different possible narratives goes on.

In our view, this speaks to how critical it is to adhere to an underlying investment philosophy and methodology. Rather than be subject to "the slings and arrows of outrageous fortune" when being caught jumping between prevailing narratives and defining things in the manner that others are defining for you, it is clarifying to bring one's own values and approach to investment management.

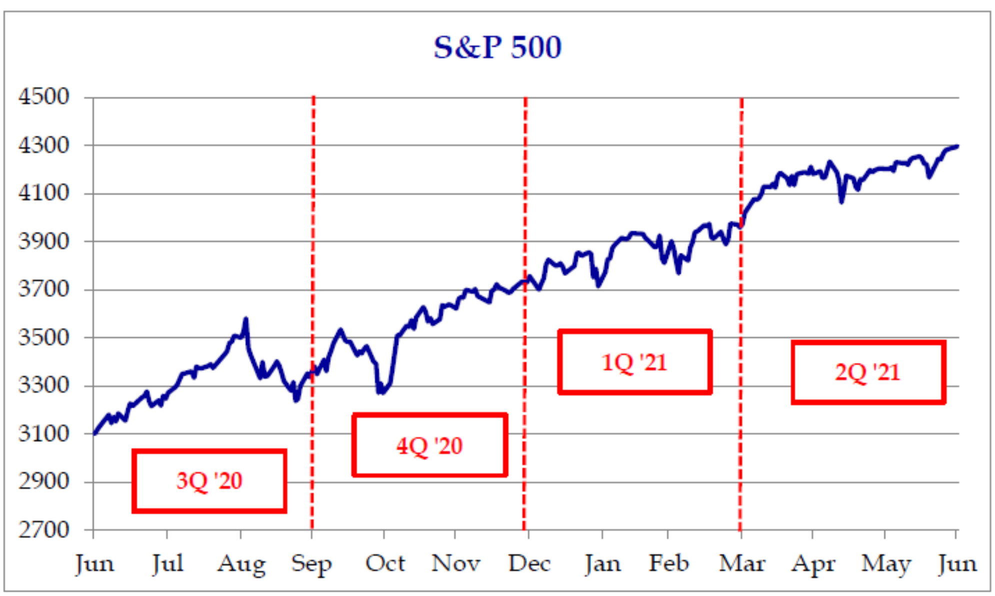
For us, it has always been about the quality of the business. It has always been about the underlying growth in the portfolio's earnings and cash flows. And it has always been about valuation as well. It is not about growth versus value…it is growth and value.

**Investment Viewpoint**

In his July 5, 2021 Weekly Economic Report, economist Ed Hyman of Evercore ISI recently noted that:

1) Consumer Net Worth has surged.
2) Consumer excess saving is over $2 trillion!
3) Monetary stimulus is unprecedented.
4) The expansion is becoming self-sustaining.
5) Foreign economies are lifting U.S. growth.
6) Reopenings will continue around the world.
7) Child Tax Credit checks could provide a significant lift to growth.

In addition, jobs are growing, and U.S. consumer confidence has rebounded. This is fueling strong earnings growth, and a steadily advancing S&P 500.




*Source: Used with permission of Strategas Research Partners as of 7/1/2021.*

Perhaps it is not surprising that there has been a surge in equity inflows during the first half of the year.

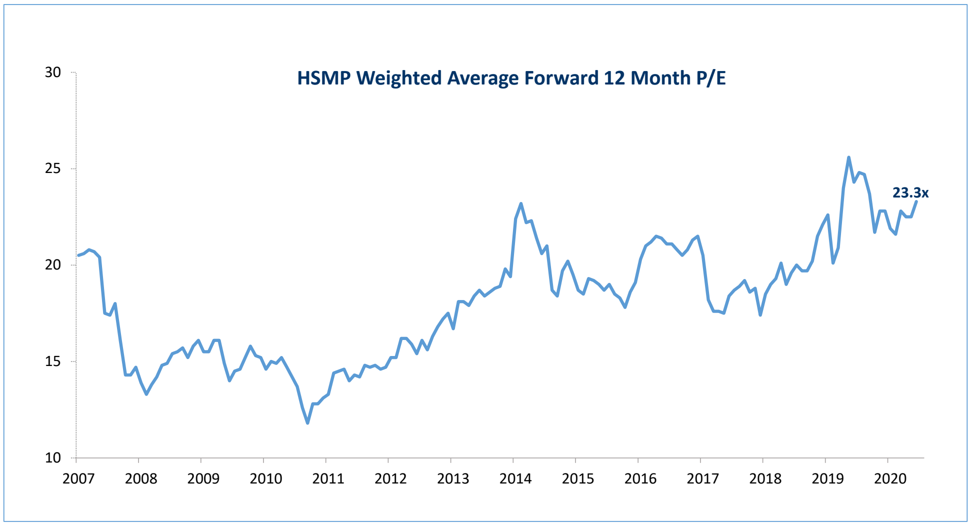

*Source: Financial Times as of 7/5/2021.*

The Cars once intoned "Let the Good Times Roll," but we cannot help taking heed at signs of speculative behavior around us. The investment landscape has become a marketing-led, distribution-driven world around us. It is very thematic. It is increasingly retail-driven. Apple used to say, "there's an app for that." Now, a myriad of investment companies have new slogans "there's an ETF for that." SPAC's may be quieting down some, but it is still a Meme, Crypto, casino-like atmosphere. Robinhood's reward for paying an unprecedented $80 million regulatory fine is to go public (IPO).

To us, investing is not gambling. It is about owning pieces of businesses. It is about trying to properly value future earnings. It is about owing a share of future cash flows.

On these metrics, we continue to feel constructive. Earnings growth looks healthy, and we may well be underestimating the absolute level of forward earnings power given the favorable economic prospects cited earlier. And while the P/E on forward earnings estimates has moved up to more than 23X at the end of the second quarter, we still think it looks appealing relative to other long duration quality assets.

HSMP Weighted Average Forward 12 Month P/E



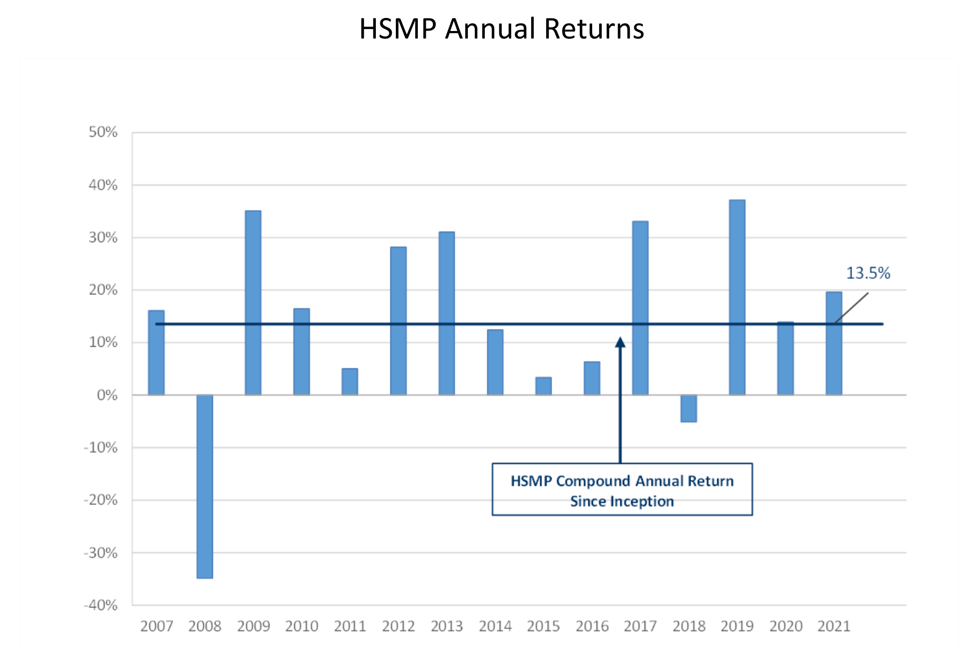

*Based on HSMP estimates since inception (4/1/07) through 6/30/21.*

Which brings us back to where we started…the ten-year bond yield. Currently, the portfolio's earnings yield (the inverse of the P/E ratio) stands at an estimated 4.3%, which looks pretty good in a roughly 1.5% bond yield world. The dividend alone on the portfolio at 1.4% approaches that level and is sharply higher than one could get in any short-term vehicle (savings accounts get you a lousy 5 bps!)

We still think there is a good possibility that we see higher interest rates as the economy strengthens, inflation works its way through the system, and as the Fed begins to lessen Quantitative Easing (QE). As we have seen in the past, removing accommodation is not easy and has led to taper tantrums around the world. From our perspective, we must be mindful that the possibility of higher bond yields can curb valuations and create dislocations in the market.

So, we remain vigilant. While we do see speculation and outsized risk away from us, we like what we own, continue to find new opportunities, and feel the valuation — while higher — is still reasonable.

As we have stated before, we have seen the growth in our portfolio earnings drive our portfolio values over time and we continue to believe that prospects for portfolio appreciation will largely be driven by earnings gains.




*Composite performance (net-of-fees) since inception (4/1/07) through 6/30/21. Performance results include the reinvestment of dividends and other earnings. Past performance is not indicative of future results. Please refer to the Performance Notes and the Additional Disclosures on pages 6-8 for important information.*

Thanks, as always, for your confidence in us. We hope everyone has a happy and healthy summer.

Sincerely,

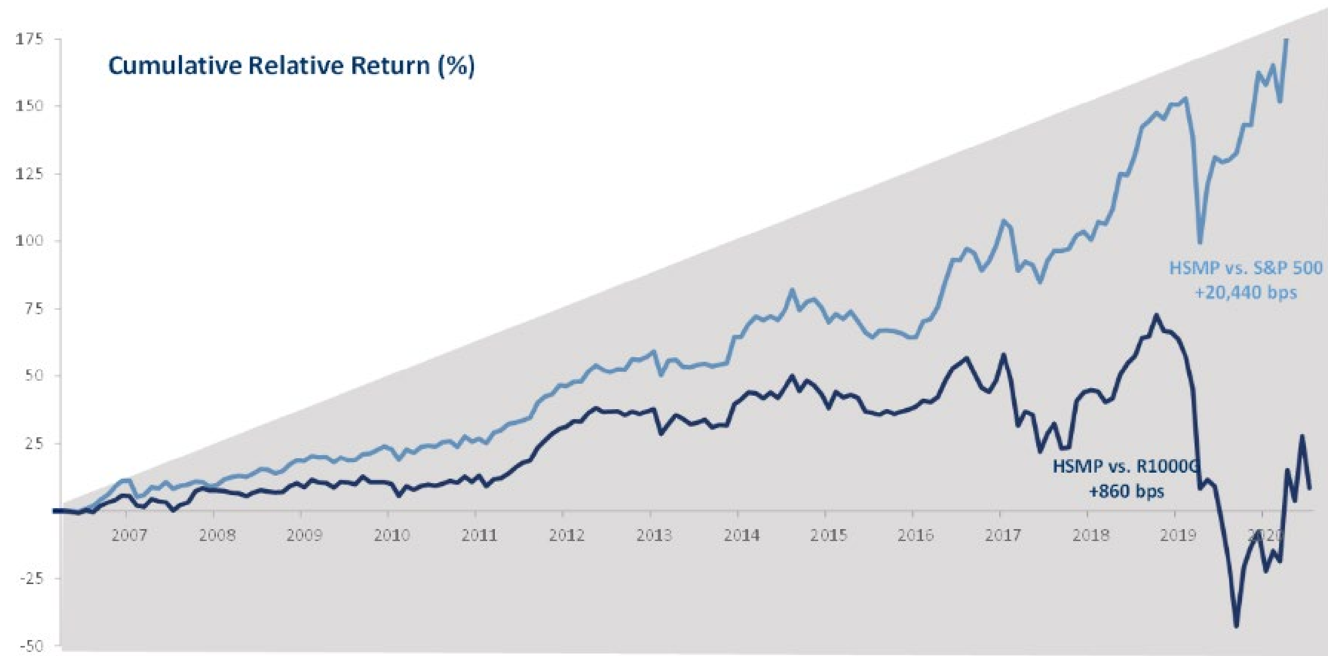
Harry W. Segalas

## *Portfolio Profile (6/30/21)*

**HSMP Composite Performance as of 6/30/21**

| | 2Q21 | YTD | 1 Year | 3 Years *Annualized* | 5 Years *Annualized* | 10 Years *Annualized* | *Since Inception 4/1/07 Annualized* | *Since Inception 4/1/07 Cumulative* |
|---|---|---|---|---|---|---|---|---|
| HSMP Composite (Net) | 10.5% | 19.6% | 46.2% | 22.0% | 20.1% | 17.1% | 13.5% | 510.9% |
| S&P 500® Index | 8.6% | 15.3% | 40.8% | 18.7% | 17.7% | 14.8% | 10.3% | 306.5% |
| Russell 1000® Growth Index | 11.9% | 13.0% | 42.5% | 25.1% | 23.7% | 17.9% | 13.4% | 502.3% |

*Performance results are net of fees and include the reinvestment of dividends and other earnings. Past performance is not indicative of future results.*




*Composite performance results since inception (4/01/07) through 6/30/21. Performance is net of fees and include the reinvestment of dividends and other earnings. Past performance is not indicative of future results.*

**IMPORTANT DISCLOSURES**

When we use *HSMP*, *HS Management Partners*, or *Firm*, we mean HS Management Partners, LLC. This piece is written from the perspective of our Composite holdings, performance, and estimated metrics, and it does not refer to any specific client account (client accounts can have higher or lower performance than that shown here and can have some but not all of the holdings shown here). When we use Composite, we mean our HS Management Partners Concentrated Quality Growth Composite, and when we use our portfolio(s)/your portfolio(s), we mean client portfolios in general from our Composite perspective (see below regarding differences between the Composite and client portfolios/accounts and differences between client portfolios/accounts themselves). This piece represents our opinion as of 7/12/2021 based on our understanding of market conditions and publicly available information (the portfolio's estimated earnings yield 4.3% figure and the 1.5% bond yield world indication are both as of 6/30/2021). It has forward-looking statements that are by their nature uncertain and based on our assumptions (such as when we refer to possible/future/estimated earnings, cash flows, earnings-per-share (EPS), growth rates, price-earnings ratios (P/E), market conditions, or portfolio/client portfolio outlook); there is no assurance that forward-looking statements will prove to be accurate as actual results and future events can differ materially from our assumptions. Some of the charts in this piece were obtained from the indicated third-party sources which we believe reliable, but we did not verify, nor do we guarantee the accuracy of this information. The performance shown should not be taken as an indication of how the Composite or a client account will perform in the future; past performance is not indicative of and does not guarantee future results. Investing in securities involves significant risks, including the risk of loss of the original amount invested. The information here is solely for illustration/discussion, is subject to change without notice, should not be construed as a recommendation to buy or sell any particular security, and should not be used as basis for making investment decisions.

HSMP claims compliance with the Global Investment Performance Standards (GIPS®). HS Management Partners, LLC is an independent SEC registered investment adviser (SEC registration does not imply any certain level of skill or training). The HS Management Partners Concentrated Quality Growth Composite includes all fully discretionary, actively managed, fee paying accounts (accounts that pay us an investment advisory fee even if they pay zero trading commissions) which employ our style of investing in 20-25 quality growth businesses. These accounts must have a market value exceeding $500,000 at the time of initial inclusion in the Composite and have a market value exceeding $300,000 to maintain inclusion. The U.S. Dollar is the currency used to express performance. For more information or for a copy of our fully compliant GIPS® Report and/or list of composite descriptions, please contact us at 212-888-0060.

Composite performance is presented net-of-fees (net of actual investment advisory fees and trading costs). The Composite is compared to the Russell 1000® Growth Index and the S&P 500® Index as benchmarks for market context only. The Russell 1000 Growth Index is an unmanaged index that measures the performance of those Russell 1000® Index companies (largest 1,000 U.S. companies based on market capitalization) with higher price-to-book ratios and higher forecasted growth values. The S&P 500® Index is an unmanaged market capitalization-weighted index designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. There are meaningful differences between the Composite and each index that should be considered when comparing performance, such as in terms of composition, concentration and volatility (e.g., the Composite contains securities not represented in either or both indices and is much more concentrated than either index in terms of companies and sectors; the average market capitalization of companies in the Composite will likely differ from that of either index; and market or economic conditions can affect positively/negatively the Composite's performance but not the indices to the same extent). In addition, neither index bears fees and expenses and investors cannot invest directly in either of them. Furthermore, we do not seek to mimic any market index in our investment approach and do not maintain limits on industry or sector weightings.

Although most discretionary client accounts are included in the Composite and dispersion is typically low over time, not all client accounts are in the Composite, and even for those in the Composite, there can be dispersion, particularly for small client accounts and also when viewed over narrow time periods. Client account holdings and performance can deviate from our Composite (and not all client accounts are in the Composite) or from other client accounts (even within the same group and even when comparing different accounts of the same client), and also from the representative portfolio, for several reasons, such as: client restrictions, account type and size, timing and market conditions at an account's inception and contributions/withdrawals, timing and terms of trades, actual client investment advisory fees (or the lack thereof), and client directed brokerage/commission recapture instructions. In fact, small accounts generally experience higher dispersion from our Composite than large accounts primarily because they do not participate in trading/allocations/aggregations to the same extent as large accounts (in addition to the mentioned reasons for client account holdings and performance dispersion, actual participation in trade orders also depends on cash available in an account and on our imposed per-order share minimums, which typically range anywhere from 5 to 100 shares depending on the stock price). Also, while the investment merits of a given security drive our investment decision, we take into consideration the tax status of an account or group of accounts in certain instances when practicable under select circumstances (that being said, we are not a tax-efficient focused adviser and do not provide tax advice, and clients should consult with their own separate tax advisors in this regard). Furthermore, under our sole investment strategy (HSMP Concentrated Quality Growth Equity strategy) we provide investment advice on a discretionary basis (we make all the investment decisions and trade the accounts) and also on a non-discretionary basis in the form of model portfolios for use in multimanager products (we act as a non-discretionary sub-adviser and do not make the final investment decisions nor trade the accounts); therefore, certain information here (including holdings, performance, Composite, and investment strategy implementation) is not applicable to model portfolio clients as we have no control and do not monitor the implementation (complete, partial or not at all) of model portfolios, and the performance of model portfolio clients is not attributable to us.

We typically build a concentrated portfolio with a hard cap on company names and with an aim to keeping clients' capital nearly fully invested. Our investment advice is limited to domestic and foreign equity securities of publicly traded companies. Client accounts generally hold 20-25 companies, although in certain circumstances they may hold more or less names. We do not maintain limits on industry or sector weightings, and while we do limit portfolio positions by company, clients' portfolios are likely to be significantly concentrated by sector, industry and/or geography, among other factors. While we believe that our investment strategy will produce desired returns, there can be no assurance that we will achieve our investment objectives. We encourage you to refer to our Firm Brochure (which is available on our website—www.hsmanage.com—or upon request at 212-888-0060) for some material risks applicable to our investment strategy and additional information regarding our Firm.

In response to COVID-19 and in an effort to protect the safety of our team and the continuity of our critical business operations (making investment decisions, trading and settlement, and communicating with clients about the status of their accounts), our employees are working remotely, and we suspended business travel and replaced in-person meetings with conference calls and video chats. We have tested our capacity to operate remotely and we believe we can continue to perform our services, assuming that conditions do not worsen dramatically, that our team and close family members do not fall ill with COVID-19, that there are no significant disruptions to our key service providers, and that our team continues to have internet connectivity and phone access from home. Although our business continuity/disaster recovery plan aims to mitigate the impact of natural disasters or catastrophic events by maintaining critical business functions while keeping the safety of our employees first, no plan can guarantee the continuity of our operations in the presence of these events.

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