DISTILLATE CAPITAL

2021 Year-End Letter to Investors: Value Below the Surface

Strategy Description

Distillate Capital's U.S. and International Fundamental Stability & Value (U.S. FSV & Intl FSV) strategies seek to outperform over the long-term by investing in stocks that are more fundamentally stable, less levered, and more attractively valued. Distillate's Small Cap U.S. Quality and Value (U.S. SQV) seeks to do the same by focusing valuation and indebtedness.

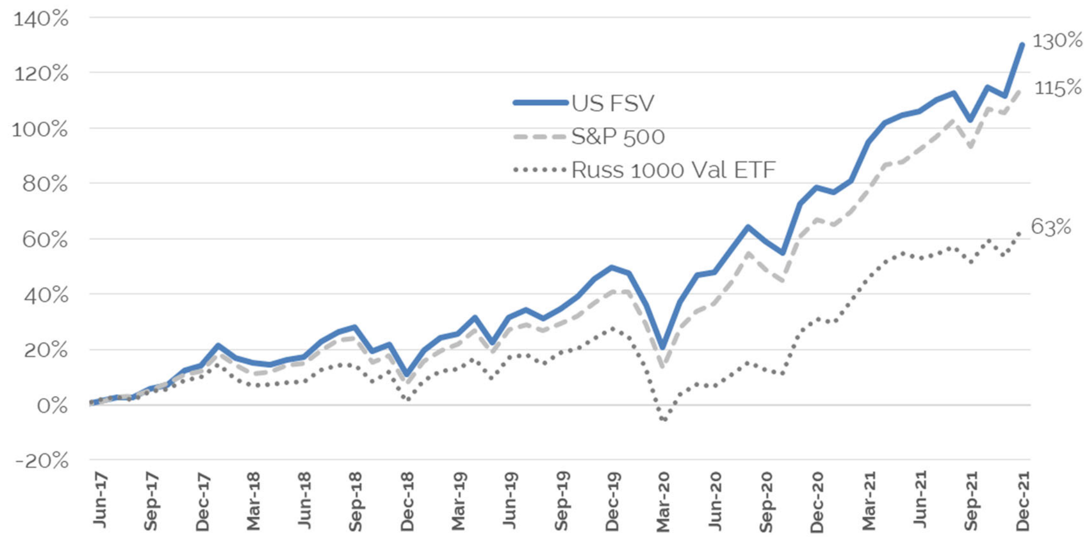
Performance Summary

U.S. Fundamental Stability & Value (U.S. FSV): Distillate's U.S. FSV strategy slightly outpaced the S&P 500 in 2021 with a return of 28.91% after fees versus 28.71% for the benchmark. Since its inception in 2017, annualized performance is now 1.80% ahead of the S&P 500 after fees and comes despite headwinds from concentrated gains among several of the largest and most expensive stocks in the benchmark. Against the iShares Russell 1000 Value ETF benchmark, U.S. FSV led by a substantial 4.00% in 2021, and annualized performance since inception is now 8.63% ahead of the benchmark. Cumulative returns are shown in **Figure 1** which highlights the strategy's total return since inception of 130% compared, to 115% for the S&P 500 and just 63% for the iShares Russell 1000 Value ETF. While our nearly five-year track record is still a brief moment in time, we believe we are building a body of evidence that value investing remains an effective investment strategy provided valuation is measured properly.

International Fundamental Stability & Value (Intl. FSV): After outperforming by 7.78% in 2020, Distillate's Intl. FSV strategy lagged its benchmark, the iShares MSCI ACWI ex-US ETF, by 5.81% in 2021, with a total return of 1.67% after fees versus 7.48% for the benchmark (See **Figure 3** on the following page). Annualized returns net of fees since inception for the international strategy remain 1.28% ahead of its benchmark.

U.S. Small Quality & Value (U.S. SQV): Distillate's U.S. SQV's 2021 total return after fees of 36.03% significantly exceeded the total return for the iShares Russell 2000 ETF of 14.64%, and the iShares Russell 2000 Value ETF's total return of 27.96%. Following significant previous gains over the benchmarks, the strategy is substantially ahead of the Russell 2000 and Russell 2000 Value, by 7.3% and 8.5%, on an annualized net-of-fee basis since inception (See **Figure 4** on the following page).

Figure 1: Since Inception Total Return for Distillate's U.S. FSV (net of fees) vs. Benchmarks



Source: U.S. Bank, Morningstar Data; See performance disclosures

Performance Charts: **Figures 2 through 4** depict annual performance for Distillate's U.S. and Intl. FSV strategies and its U.S. Small Quality Value (U.S. SQV) strategy versus their respective benchmarks since inception.

Figure 2: Performance of Distillate's U.S. FSV Strategy (through 12/31/2021)

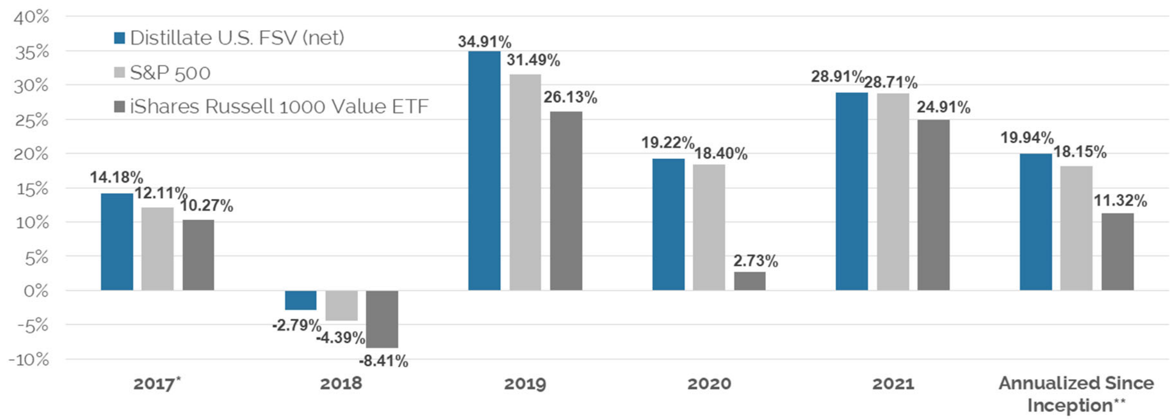


Figure 3: Performance of Distillate's International FSV Strategy (through 12/31/2021)

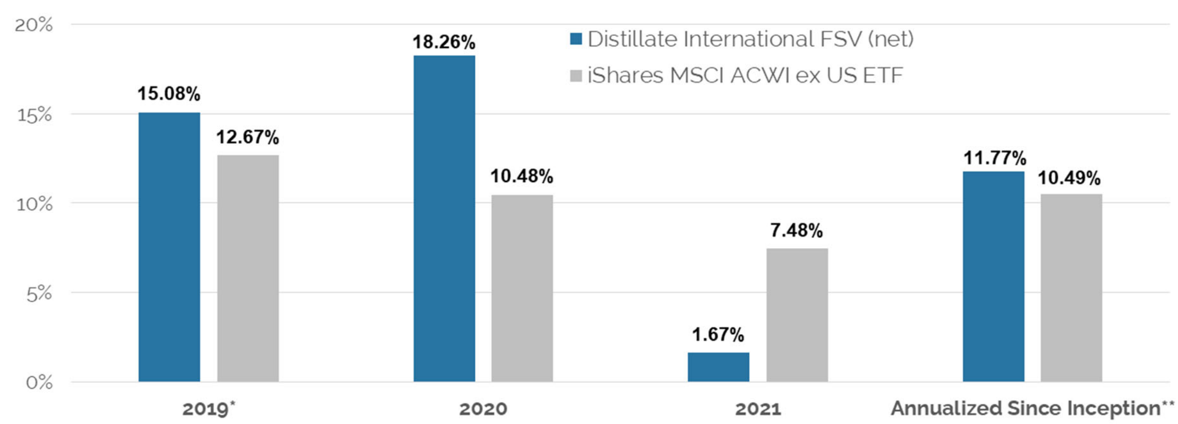
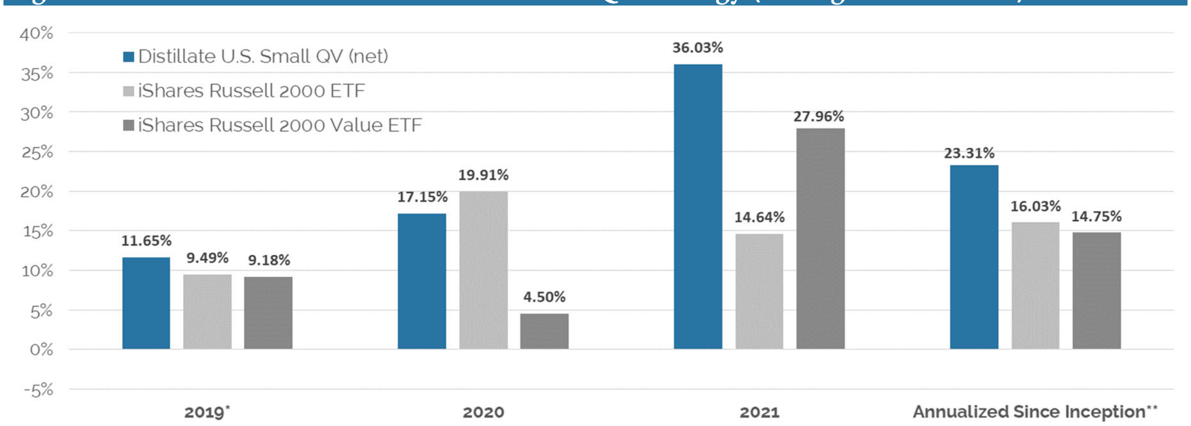


Figure 4: Performance of Distillate's U.S. Small QV Strategy (through 12/31/2021)



* Strategy inception of 5/31/2017 to 12/31/2017 for US FSV; 1/31/2019 to 12/31/2019 for INTL FSV; and 3/31/2019 to 12/31/2019 for US SQV.
** Strategy inception of 5/31/2017 for US FSV; 1/31/2019 for INTL FSV; and 3/31/2019 for US SQV.
Sources: U.S. Bank, Morningstar Data. Please see important performance disclosures at the end of this document.

Market Commentary:

Equity performance in Q4 was strong with the S&P 500 up 10.6%, driving valuations higher. The next twelve-month free cash flow to market cap yield on the S&P 500 started the fourth quarter at 4.44% and ended the year at 4.11%, placing it near the lowest level it has been since the recovery from the financial crisis began. While the overall capitalization-weighted S&P 500 has gotten more expensive, there are notable nuances below the surface that deserve consideration and explain our current positioning and somewhat more constructive outlook.

First, it is worth noting that the concentration of the largest companies in the S&P 500 has not been at current levels in most of our investment lifetimes (See **Figure 5**). We believe this presents some unique risks, not just in the level of exposure, but also considering the valuation of that group of stocks, which collectively have a free cash flow yield one-third less than the overall market, which they heavily influence. For further detail, see our recent one-page paper on the topic (Concentration Risk.)

Concentration in the S&P 500 Index is extremely elevated.

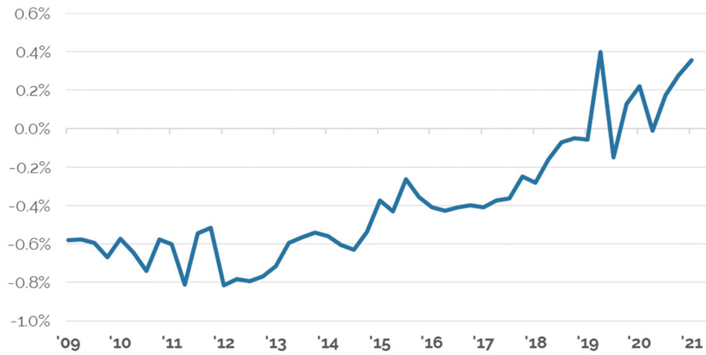
Figure 5: Top 5 Stock Share of S&P 500 Index

Source: FactSet; data as of 12/31/2021

Beyond the concentration and valuation of the largest five companies in the S&P 500, we note that larger companies in general are more expensive than they have been. We utilize free cash flow yields to examine the difference between the valuation of an equal-weighted S&P 500 versus the more-typical cap weighted index, and for simplicity use next-twelve-month consensus estimated free cash flows (NTM FCF) relative to enterprise value (EV). This analysis, shown in **Figure 6**, highlights that as the market came out of the financial crisis, the biggest stocks were somewhat cheaper than the broader index and the free cash flow yield of the equal-weighted index was 0.6% to 0.8% lower than the cap weighted index. But as the largest stocks steadily became more expensive and especially so recently, the average company changed position and now has a free cash flow yield that is 0.4% above that of the overall cap-weighted S&P 500. Said differently, the relative positioning of the two groups on a valuation basis has shifted meaningfully.

The equal-weighted S&P 500 now offers a higher free cash to enterprise value yield and is cheaper than the traditional cap-weighted index.

Figure 6: Free Cash to EV Yield of the Equal Weighted S&P 500 Less the Cap-Weighted Index

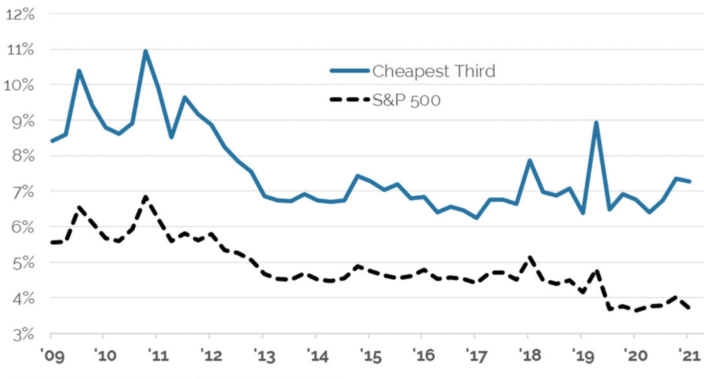


Source: FactSet; See endnotes for methodology details.

While the steady upward rerating of the biggest stocks has driven the overall market and left fewer compelling opportunities among the largest companies, looking beyond the mega-caps, levels have changed very little among the least expensive stocks. **Figure 7** depicts the least expensive one-third of the constituents of the S&P 500 versus the overall market. The free cash flow yield of the cap-weighted index (utilizing enterprise value as the denominator) hovered around 4.5% from 2013 to 2018 until falling to 3.7% as of the end of the year. The cheapest third of the market, by contrast, has yielded around 7% since 2013, and actually increased most recently when the overall market free cash to enterprise value yield fell.

While the overall S&P 500 valuation has gotten richer, stocks in the cheapest third of the market have remained cheap.

Figure 7: Free Cash to EV Yield of the Cheapest Third of the S&P 500 vs. the Overall Index



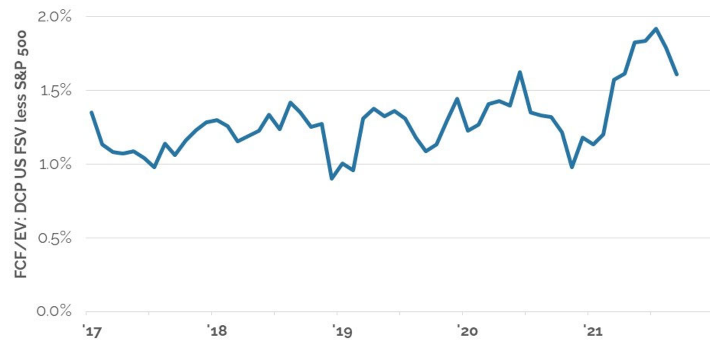
Source: FactSet; See endnotes for methodology details.

Better yields in smaller companies within the S&P 500 (though still quite large) is consistent with our shift away from some of the biggest and most expensive stocks in recent quarters. Importantly, this does not mean sacrificing quality, as our measures of fundamental stability and financial leverage among held stocks has changed very little and remains strong.

Consistent with this market shift, the valuation spread of Distillate's U.S. FSV strategy has widened relative to the S&P 500 Index. **Figure 8** shows Distillate's U.S. FSV's free cash flow to enterprise valuation yield spread over the S&P 500, that notably has expanded in the most recent period without a corresponding shortfall in overall performance. A similar dynamic has played out internationally, as seen in **Figure 9**. Further commentary on valuation and quality follows on pages 5 and 6 in the standard discussion of how our strategies compare on each attribute versus their relative benchmarks.

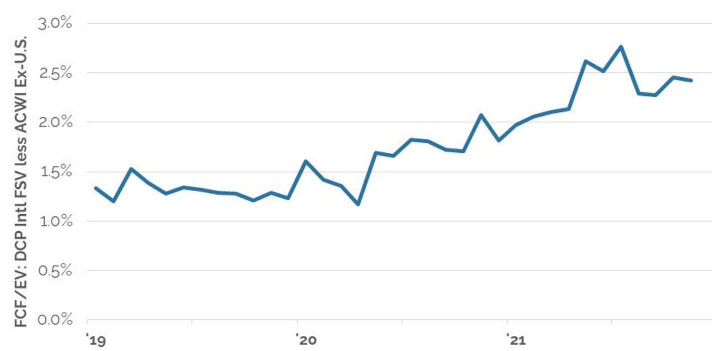
Distillate's U.S. and International FSV strategies have seen their cash flow yield valuations recently improve relative to respective benchmarks.

Figure 8: Free Cash to EV Yield: Distillate's U.S. FSV Strategy Less the S&P 500 Index



Source: FactSet, See end-notes for methodology. As of 1/14/2022

Figure 9: Free Cash to EV Yield: Distillate's Intl. FSV Strategy Less the MSCI ACWI Ex-U.S. Index

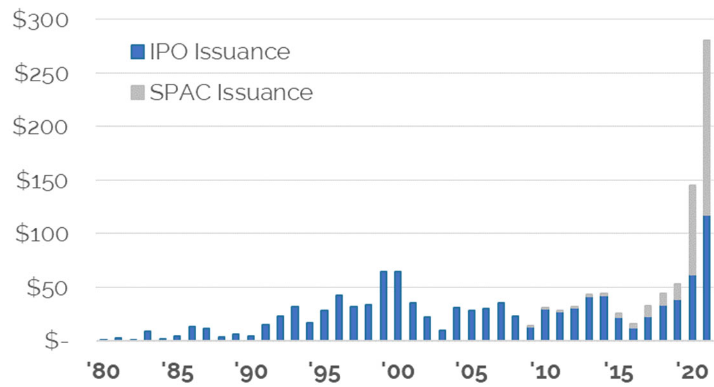


Source: FactSet, See end-notes for methodology. As of 1/14/2022

Free cash flow yields beyond the largest names and the yield spread we are able to compile in our holdings versus the market weighted benchmark leave us feeling better than much of the market commentary that we see might suggest we should. But pockets of concern are evident elsewhere and we believe should be avoided. Worth noting in 2021, there was a massive surge in listings of new companies, utilizing both the traditional initial public offering (IPO) market, as well as via a newer vehicle, those known as special purpose acquisition companies (SPACs). **Figure 10** looks at the combination of these two routes to market and highlights the enormous amount of capital that has flowed into newly listed stocks.

Combined figures for traditional Initial Public Offerings and SPAC issuance show a massive surge in committed capital.

Figure 10: Traditional IPO and SPAC Issuance

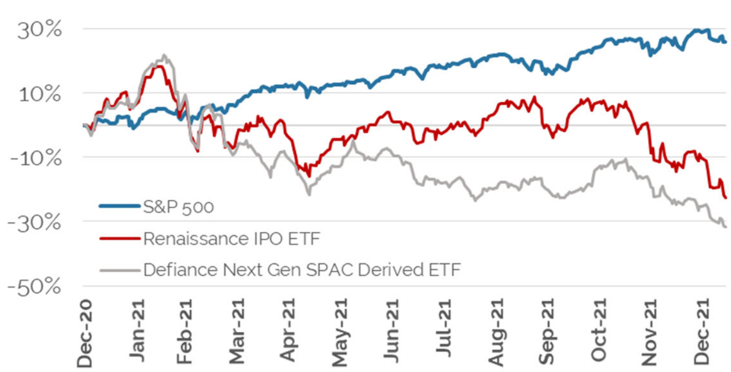


Source: Jay Ritter, University of Florida, IPO Statistics & SPACinsider.com

The amount of capital devoted to new public issuance in 2020 and 2021 was truly staggering, well outpacing the cumulative prior decade of similar activity. Floods of capital tend to dampen returns and results in 2021 proved no different. Note in **Figure 11** the performance of two ETF's structured to track the new issuance markets. Both "SPAK", the ETF designed to track a basket of SPAC companies, as well as "IPO" the IPO-version of the same concept, substantially underperformed the S&P 500 Index last year.

Amid the enormous issuance of new capital from IPOs and SPACs, ETFs that Invest in such stocks (SPAK & IPO) have lagged significantly.

Figure 11: Total Return of SPAC and IPO Focused ETFs vs. the S&P 500 (12/31/20-1/14/22)



Source: FactSet

Even as many SPACs and IPOs have lagged the market (and interestingly, roughly 30% of all NASDAQ stocks are 50% down from their 52-week highs as of January 14^{th}, 2022) there remains a notable and headline generating list of very richly valued stocks that have many market commentaries expressing significant concern.

Table 1 highlights a number of these companies, including many that were recently listed, that trade at extreme multiples of sales and free cash flows. In aggregate, this list has a market capitalization of nearly $3.5 trillion against expected next-twelve free cash flows of less than $30 billion, or a yield of less than 1%. The aggregate price to free cash flow multiple for this group is 116x compared to 24x for the market overall, a level that in our estimation creates an enormous hurdle for growth to overcome in order to generate positive returns for shareholders. Perhaps stating the obvious, we own none of these shares.

Price-to-Sales and Price-to-Free Cash Flow among some of the largest headline grabbing companies in the U.S. Equity market

Table 1: Richly Valued Stocks

Name	Market Cap.	Sales (NTM Estimate)	Free Cash Flow (NTM Estimate)	Price to Sales	Price to Free Cash Flow
Tesla	$ 1,061,287	$ 73,946	$ 6,554	14.4	162
NVIDIA	$ 735,275	$ 31,175	$ 11,938	23.6	62
Netflix	$ 266,852	$ 34,074	$ 1,132	7.8	236
Salesforce	$ 250,318	$ 31,332	$ 6,105	8.0	41
Shopify	$ 173,001	$ 6,110	$ 778	28.3	222
ServiceNow	$ 129,173	$ 7,377	$ 2,292	17.5	56
Airbnb	$ 105,786	$ 7,364	$ 1,726	14.4	61
Snowflake	$ 103,759	$ 1,931	$ 185	53.7	561
Rivian	$ 93,354	$ 3,249	$ (6,988)	28.7	(13)
Uber	$ 81,349	$ 25,307	$ 831	3.2	98
Snap	$ 75,709	$ 5,570	$ 571	13.6	133
Lucid	$ 62,644	$ 2,062		30.4	
Roblox	$ 59,713	$ 3,327	$ 574	17.9	104
DataDog	$ 55,573	$ 1,406	$ 233	39.5	239
Zoom Video	$ 54,804	$ 4,695	$ 1,583	11.7	35
Coinbase	$ 54,311	$ 7,247	$ 1,555	7.5	35
DoorDash	$ 51,081	$ 6,036	$ 346	8.5	148
Sum	*$ 3,413,989*	*$ 252,206*	*$ 29,416*	*13.5*	*116*
S&P 500*	$ 4,766	$ 1,668	$ 196	2.9	24

*Per share data
Source: FactSet Data, as of 12/31/21

Overall, there are some extremes in the market, generating typical doom-saying headlines and dramatic shifts in outcomes for some notable asset managers and hedge funds. That said, we do not invest in "the market", but take a selective approach, and in our estimation, and perhaps explaining a good part of the market's continued overall strength despite some notable corrections, there remains ample opportunity below the surface.

Valuation & Quality vs. Indexes

As we highlighted last quarter, we believe the valuation and quality charts on the following pages depict the most relevant metrics for evaluating our strategies and for understanding how they differ from comparable indexes.

Starting with valuation, **Figure 12** compares next-twelve-month estimated free cash flows to enterprise value and highlights substantial valuation advantages for each of Distillate's strategies compared to their relevant benchmarks. This measure is slightly different from the normalized free cash flow yield methodology that we use to value individual stocks, but is straight-forward and comparable across a variety of benchmarks. The yield differential of the U.S. FSV strategy over the S&P 500 Index is significant, as noted earlier, but the yield over that of the Russell Value ETF is also high despite that index's significant underperformance.

Figure 13 looks at fundamental stability by assessing the through-cycle variability of cash flows, with a higher score equating to greater stability. It is the same metric used for stock selection in the FSV strategies. The greater stability available through stock selection versus benchmark in our estimation are meaningful and particularly important to our goal of preserving capital in adverse scenarios. The small cap strategy does not employ a stability overlay since we have found this metric to be less useful in the small cap space where companies tend to have shorter histories and much less stability in general.

Figure 14 measures leverage in the form of total debt relative to normalized lease-adjusted consensus estimates for earnings before interest, taxation, depreciation, and amortization (EBITDA). Leverage for the U.S. FSV strategy is not that differentiated from the S&P 500 benchmark where many mega-cap companies with little debt have a significant impact on the overall level of indebtedness. The goal of employing a leverage limit is not necessarily to have less leverage than the overall index, but to select stocks that will preserve capital in challenging economic environments. Internationally, leverage is higher in the benchmark than it is domestically and the international FSV strategy is much more differentiated in this regard. Lastly, leverage is very high among small cap companies despite the fact that the fundamentals for these companies are more volatile and they are thus less able to support higher debt burdens. We believe this is a key risk among smaller companies and an attribute that is crucially differentiated in our small cap strategy versus benchmarks.

Given this backdrop of richer valuations in the U.S., lower quality and higher leverage internationally, and low valuations and very high debt levels among smaller U.S. stocks, we continue to see significant potential benefits to stock selection and avoiding these risks in each of the U.S. large cap, international, and U.S. small cap spaces.

Positioning: **Figure 12** shows the current valuations for Distillate's U.S. and International Fundamental Stability and Value (FSV) strategies and its U.S. Small Quality and Value versus various benchmarks. **Figure 13** compares the same Distillate strategies and corresponding benchmarks on our cash flow stability scores, and **Figure 14** examines the degree of financial leverage across the same strategies and benchmarks.

Figure12: Next 12-Month Free Cash Flow to Enterprise Value

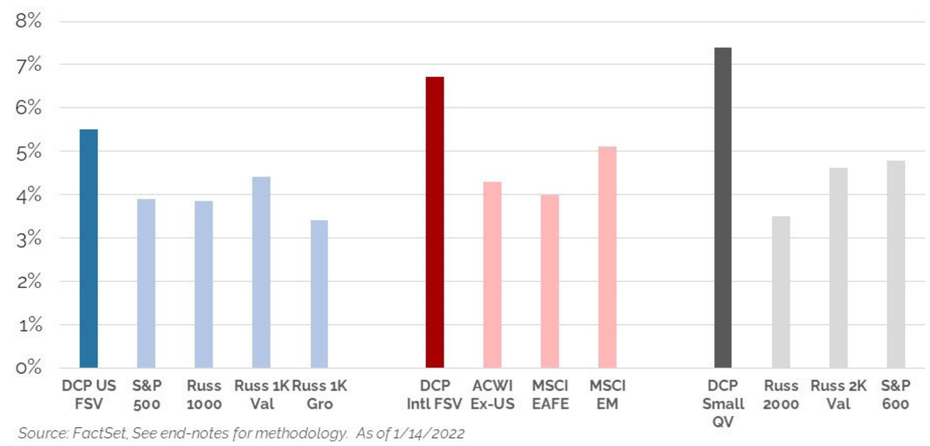


Figure 13 (Quality): Distillate's Cash Flow Stability Score

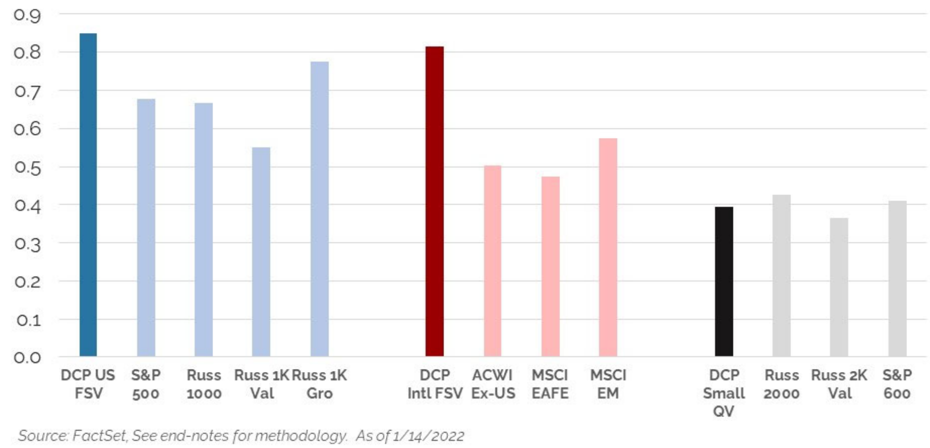
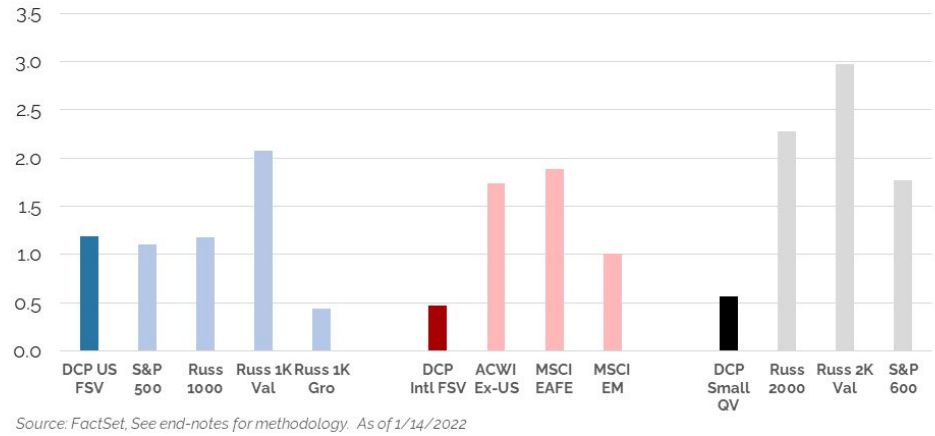


Figure 14 (Quality): Net Debt to Adjusted EBITDA



Performance

U.S. Fundamental Stability & Value (U.S. FSV)

In 2021, Distillate's U.S. FSV strategy outpaced the S&P 500 benchmark by around twenty basis points despite the challenging headwind from strong gains and expanding valuations among several of the biggest stocks in the index. For example, the relative drag on performance from not owning Microsoft and Nvidia was 2 percentage points and Tesla detracted another 33 basis points incrementally.

Among owned positions, Arista Networks, Lam Research, and Oracle were the strongest contributors versus the S&P 500 benchmark, adding around 40 basis points each to relative performance. Activision Blizzard, Citrix, and Viatris, by contrast, were the worst contributors to relative performance with each subtracting around 40 basis points in relative performance.

By sector, the underweight in financials, where leverage tends to limit the portfolio weight, was a 0.2% drag versus the benchmark and the overweight in the industrials and consumer staples each subtracted another 0.5%. The underweight in energy, where high cash flow volatility and leverage make many of the stocks look unappealing from a risk point of view, detracted another 0.6%. A total of roughly 2 percentage points of drag from sector selection was more than offset by individual stock selection, with the result being slightly positive overall relative performance for the year. As a reminder, sector weights are driven by bottom-up stock selection and reflect the attractiveness of the stocks within the sector on the basis of free cash flow valuation and quality.

International Fundamental Stability & Value (Intl. FSV)

After outperforming the iShares MSCI ACWI Ex-US ETF benchmark by around 8% last year, the International FSV strategy lagged the benchmark by 5.81% in 2021 **(See Figure 2)**.

Underperformance in 2021 can be broken down into three main issues. First, Chinese stocks were a substantial ~2.5% drag on relative performance. Our holdings in any region are capped to 150% of the benchmark region weight, with the intention of limiting our exposure to particular regions and countries. And in China, this limit is based on tradable securities in the Hong Kong market, which roughly limits our China exposure to 13%, or approximately the weight China commands in aggregate in the overall benchmark. Nonetheless, sharp declines in several Chinese holdings impacted by government policy changes imposed a significant drag on performance. Second, strong performance of financial stocks, and bank stocks in particular, also contributed another ~2% to the shortfall versus the benchmark. As a reminder, high leverage, low stability, and lacking free cash flows will limit ownership in financials in our International FSV strategy. In general, sector weights should not have an outsized impact on performance for the strategy over time. That said, the strategy's general aversion to owning bank stocks for the reasons noted above will lead to an underweight in this industry, which is much larger in the international benchmark than it is domestically. The international strategy may therefore vary in performance on a quarter-to-quarter basis more than is the case domestically if bank stocks are rising or falling sharply. Over time, given the goal of protecting capital, we believe the general lower exposure to balance-sheet-driven financials makes sense and we believe this to be especially true internationally where many banks are captive to local governments and not necessarily run for the benefit of shareholders. Lastly, the portfolio has lagged the benchmark by roughly 2 percentage points due to performance in the metal and mining industry. This resulted from an underweight in certain mining and steel stocks that rose sharply in 2021, and underperformance among several precious metal miners that were owned. The unowned mining and metal stocks have a legacy of volatile fundamentals, and some are financially levered as well and therefore not constituents in our portfolio. Our objective is that the performance drag that may come from not owning such stocks in a rising market will be more than offset by the capital preservation benefit of avoiding them during periods of inevitable distress. deleted last thought that was here.

We are disappointed with the extent of this year's underperformance and that it has offset some of the very strong relative gains from last year. Still, we are encouraged by the free cash flow yield over that of the benchmark at present and continue to firmly believe that focusing on leverage and financial stability are crucial to preserving capital and limiting losses, allowing capital to compound at better than market returns over the long run. Given the higher financial and metal and mining weights in the international benchmark, greater variability around that index is to be expected compared to the U.S. strategy and the performance in 2020 and 2021 is consistent with this view.

U.S. Small Quality & Value (U.S. SQV)

Performance for Distillate's U.S. SQV strategy significantly exceeded that of both the iShares Russell 2000 ETF and the iShares Russell 2000 Value ETF benchmarks, with gains over those respective benchmarks of more than 21% and 8%, respectively in 2021 net of fees. Cumulative annualized performance is now 7.3% and 8.6% ahead of the same benchmarks since inception in 2019. Top contributors in 2021 include Signet Jewelers and PBF Energy, which each added around 1.5% to relative performance and Consol Energy, ArcBest Corporation, and Vertiv, which each added approximately 1% to relative performance versus the Russell 2000 ETF benchmark. The largest detractors from relative performance were Tupperware Brands and Green Dot Corporation, which each subtracted about 0.4% from relative performance. Several unowned "meme" stocks such as GameStop and AMC Entertainment, which ended the year up over 1,000%, and Avis Budget Group which returned nearly 500%, combined to weigh on relative performance by almost a full percentage point.

Portfolio Changes & Valuation

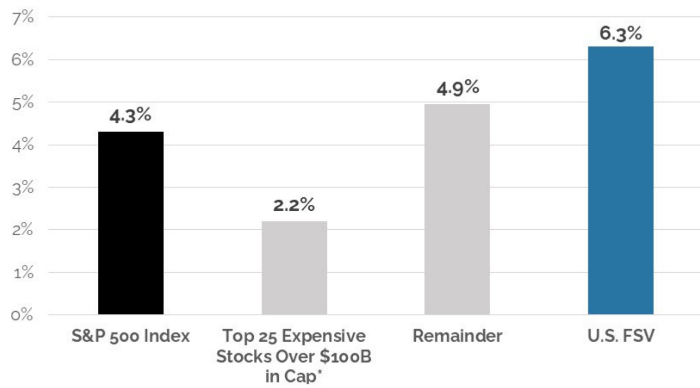
U.S. Fundamental Stability & Value (U.S. FSV)

After rebalancing, the weighted average free cash flow yield to market cap for the U.S. FSV strategy is 6.3% versus a comparable 4.3% for the S&P 500, and the free cash flow to enterprise value yield is 5.5% vs. 3.9%.[1] Both metrics are near their highest positive spread over benchmarks since the strategy's May 2017 inception. As discussed previously, we believe this reflects both a wide dispersion in valuation opportunities as well as the depressive impact of several large richly valued stocks on the overall market. This latter point is evident in **Figure 15** which contrasts the free cash to market cap yield of Distillate's U.S. FSV strategy with that of the S&P 500. The figure shows the large downward pull of the most expensive 25 stocks with market values over $100 billion, which collectively have a free cash yield of just 2.2%. If those stocks are removed from the analysis, the free cash flow yield on the remainder rises to 4.9%, providing a reasonable starting point with which to select attractive stocks.

In addition to the valuation advantage to the market, Distillate's U.S. FSV strategy also enjoys significantly more stable long-term fundamentals, as evidenced by the higher fundamental stability score in **Table 2**. Also shown, the FSV strategy has a comparably low level of indebtedness to the market, though this metric excludes a number of financials where forward estimates for EBITDA are not available and so likely flatters the index figure.

Distillate's U.S. FSV strategy is avoiding several large richly valued stocks that are driving the overall S&P 500 free cash yield lower.

Figure 15: Free Cash to Mkt Cap Yield for the S&P 500, 25 Large Expensive Stocks, & Distillate's FSV



Source: FactSet, 1/14/2022
Stocks without estimates are excluded and the index re-weighted

Distillate Capital's U.S. FSV Strategy is less expensive, more fundamentally stable, and comparably levered than the S&P 500.

Table 2: U.S. FSV Portfolio Characteristics*

	U.S. FSV	S&P 500
Free Cash Yield to Mkt Cap[1]	6.3%	4.3%
Free Cash Yield to EV[1]	5.5%	3.9%
P/E[2]	17.0	25.5
Fundamental Stability[3]	0.85	0.68
Leverage[4]	1.19	1.10

*as of 1/14/2022

Sector Changes: the largest sector change was an approximate 3% reduction in both the technology and industrials sectors. Offsetting this was a 4% increase in consumer staples and a 1.5% increase in financials. Sector weights reflect the opportunity set at the stock level and are not driven by any top-down decisions or limitations. The opportunity set presently favors the industrials, health care, consumer discretionary (ex AMZN & TSLA), and technology (ex AAPL & MSFT) sectors where valuations look attractive, and leans away from financials and communications. The consumer staples weight has also been rising recently after the underperformance of many stocks in that sector (**See Table 3**).

Sector weights are driven by bottom-up stock selection which currently favors the Industrials and health care sectors versus the S&P 500 Index.

Table 3: U.S. FSV Sector Exposure*

	U.S. FSV	S&P 500
Communication Services	5.5%	10.2%
Consumer Staples	11.5%	6.0%
Consumer Discretionary	13.7%	12.3%
Ex Amazon & Tesla	*13.7%*	*6.6%*
Energy	1.1%	3.2%
Financials	4.1%	11.4%
Health Care	20.5%	12.9%
Industrials	18.5%	7.9%
Information Technology	19.4%	28.4%
Ex Apple & Microsoft	*19.4%*	*15.7%*
Materials	4.9%	2.6%
Real Estate	0.8%	2.6%
Utilities	0.0%	2.5%

*as of 1/14/2022

[1] Free Cash Yield to Market Cap and Enterprise Value (EV) are based on the next-twelve-month free cash flow estimates relative to market capitalization and EV, which adds Distillate's proprietary measure of indebtedness. Stocks without estimates in the are excluded and the remaining names are reweighted based on those exclusions.
[2] P/E is based on consensus estimates for next-twelve-months and excludes P/Es over 250 and under 0 to avoid the distortion from outliers.
[3] Fundamental stability is Distillate Capital's proprietary measure of through-cycle cash flow stability with a higher value indicating greater stability.
[4] Leverage is based on Distillate Capital's proprietary measure of indebtedness which looks at the ratio of adjusted net debt to an adjusted measure of forecast Earnings Before Interest, Taxation, Depreciation, and Amortization (EBITDA.)

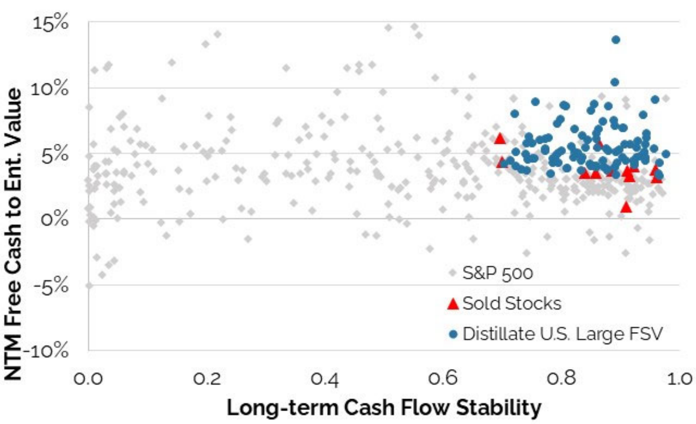
Sells: The largest exited position in the quarter was Meta Platforms (formerly Facebook), which underperformed the market but saw significant deterioration in its projected free cash flow such that its valuation became less attractive. The next biggest sales were Accenture, Intel, and Arista Networks. Accenture and Arista both outperformed significantly while Intel, like Facebook, lagged in relative performance but saw its projected free cash flows decline amid significantly increased capital expenditure plans such that its valuation declined.

Buys: The largest new purchase was Alphabet, which underperformed modestly in the quarter but substantially outperformed in the year. It was purchased despite this outperformance as its estimated normalized free cash flows have increased considerably such that its valuation now warrants inclusion. Walmart and Texas Instruments were also among the largest new positions, where each underperformed last quarter and saw their relative valuations improve. CVS was added as well, despite modest outperformance last quarter as its debt burden has fallen below the criteria for inclusion.

Summary of Holdings vs. the Benchmark: Similar to our prior presentations, one way to visualize the current portfolio versus the benchmark, as well as noting the recent changes, is to look at scatter plot of all of Distillate's FSV holdings versus those in the benchmark (**See Figure 16**) with valuation on the vertical axis and free cash flow stability on the horizontal axis. The index stocks in grey are scattered across both axes, while FSV's stocks (blue circles) are clustered to the upper right where attractive valuations and high levels of fundamental stability converge. Positions that were sold (red triangles) generally shifted to the left or fell below this cluster having become less attractively valued, but could also have been exited if debt levels exceeded the threshold for inclusion. New purchases are included among the owned stocks.

Distillate's holdings are clustered where attractive valuations and high levels of stability converge while benchmark stocks are more scattered.

Figure 16: Valuation vs. Stability for all Stocks in the S&P 500 vs. Distillate's Large Cap FSV Strategy



Source: FactSet, Reflects 1/6/22 rebalancing

International Fundamental Stability & Value (Intl. FSV)

After rebalancing, Distillate's International FSV strategy offers a higher free cash flow yield both to market cap and EV and has substantially more stable fundamentals and less leverage than the index (**See Table 4**). The international FSV strategy is thus significantly differentiated from its benchmark not just on valuation, but critically on quality as well.

Distillate Capital's International FSV Strategy is less expensive, more fundamentally stable, and less levered than the benchmark All Country World Ex U.S. (ACWI-EX US) Index.

Table 4: International FSV Portfolio Characteristics*

	Intl. FSV	ACWI Ex-US
Free Cash Yield to Mkt Cap[1]	7.4%	5.4%
Free Cash Yield to EV[1]	6.7%	4.3%
P/E[2]	15.6	20.7
Fundamental Stability[3]	0.81	0.50
Leverage[4]	0.47	1.74

*as of 1/14/2022, see footnotes on previous page.

Changes & Regional Weights: The largest sale in the quarter was Richemont, the Swiss luxury goods producer which was purchased after underperforming the MSCI ACWI-EX U.S. Index in the third quarter of last year. After outperforming the benchmark by 40% in the fourth quarter, its valuation expanded such that it no longer warrants inclusion in the portfolio and was consequently sold. The largest new position is SK Hynix, the South Korean semiconductor manufacturer which lagged last year and is trading with a free cash flow to market cap yield exceeding 7%, while carrying little debt.

Regional weights after the quarterly rebalance remain fairly well matched with the ACWI Ex-U.S. benchmark. Japan is the largest overweight at 19% vs. 14% for the benchmark and reflects increasingly attractive valuations there. Europe is a modest underweight partly due to a high index weight in balance-sheet-driven financials and somewhat reflective of valuation. The China weight is roughly in line with the benchmark due to the regional limit of 150% of the tradable universe there (**See Table 5**).

Regional weights reflect bottom-up stock selection but are limited to 150% of the benchmark to limit geographic concentration risk.

Table 5: International FSV Portfolio Region Weights*

	Intl. FSV	ACWI Ex-US
Europe	40.3%	42.6%
Japan	18.9%	14.3%
China (incl. Hong Kong)	12.3%	11.1%
Asia Ex China & Japan	17.7%	18.8%
Americas	10.9%	9.7%
Middle East & Africa	0.0%	3.3%

*as of 1/14/2022 and based on headquarter location using FactSet data.

U.S. Small Quality & Value (U.S. SQV)

Strong gains among small cap stocks continued in 2021 and price indexes are now at or near record levels depending on the benchmark. While fundamentals underpinned part of the rally, valuation expansion was a significant driver and stock valuations now look significantly richer, particularly in the headline Russell 2000 (shown in **Figure 12** which contrasted valuations across all of Distillate's strategies and key benchmarks). Fortunately, like with the large cap space, there is a wide range of valuations within this segment of the market and there remains a very attractive set of opportunities below the surface of the more expensive headline numbers. Distillate's small cap strategy of 125 stocks yields 7.4% on next-twelve-month estimated free cash flows to enterprise value compared to just 3.5% for the Russell 2000 and 4.6% for the Russell 2000 Value (**See Table 6**).

Leverage is also very elevated among small cap stocks and is another key risk to consider. Distillate's small cap strategy looks to avoid this and after rebalancing has a leverage ratio of 0.6x which is significantly lower than the very elevated 2.3x and 3.0x figures of the Russell 2000 and Russell 2000 Value benchmarks (**See Table 6**). Given more volatile underlying cash flows, small cap stocks in general would be expected to have less debt than their large cap peers, yet the opposite is true and leverage looks like a key risk to avoid in the small cap space.

Distillate's U.S. Small Cap Quality & Value strategy is more attractively valued and less indebted than its Russell 2000 and Russell 2000 Value benchmarks.

Table 6: Small Cap QV Characteristics*

	SQV	Russell 2000 ETF	Russell 2000 Value ETF
Free Cash Yield to Mkt Cap[1]	9.1%	4.9%	6.8%
Free Cash Yield to EV[1]	7.4%	3.5%	4.6%
P/E[2]	14.1	26.6	21.7
Leverage[4]	0.57	2.27	2.98

*as of 1/14/2022, see footnotes on page 7.

Final Word

We founded Distillate Capital in 2017 on the premise that value investing was still effective so long as value was measured in a way that made logical sense, and that marrying value with measures of fundamental stability and leverage could reduce risk and improve long-term returns. Though it is still early and despite headwinds from market concentration and pockets of extreme valuations, we believe this thesis is intact. Most notably, the 130% return of the U.S. FSV strategy net of fees since inception in May of 2017 and the 63% return of Russell 1000 Value ETF over the same period are starkly contrasting, and to us indicate serious flaws in the what is often labeled "value" but may offer little of it (see our early 2020 paper Value Failed Because It Was Expensive). We would expect performance versus the value benchmarks to fluctuate, especially given the chronically high weight in financials in those benchmarks, but the magnitude of the shortfall of traditional value indexes in even a few short years seems to point to underlying issues with an outdated constituent selection methodology in the construction of the value benchmarks themselves. We firmly believe that value investing still works, but not if value is defined with metrics that no longer correctly assess the difference between prices and worth.

As a firm, we are fortunate to have fellow long-term investors who share this thinking and continue to see the merits of value investing. And certainly, partially as a result, client assets have grown meaningfully, to roughly $650 million over the course of the last year. We thank you for the trust you place is us.

We wish you well in 2022. And, as always, please reach out with any questions.

DISTILLATE CAPITAL

Distillate Capital Partners LLC *("Distillate"), is a registered investment adviser with United States Securities and Exchange Commission in accordance with the Investment Advisers Act of 1940. The firm's list of composite descriptions is available upon request.*

Distillate claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Distillate has been independently verified for the periods June 1, 2017 through November 30, 2018. The verification report is available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

To receive a GIPS compliance presentation and/or our firm's list of composite descriptions please email your request to ***info@distillatecapital.com****.*

The U.S. Dollar is the currency used to express performance. Returns are presented net of management fees and include the reinvestment of all income. For non-fee-paying accounts, net of fee performance was calculated using a model management fee of 0.39%, which is the highest investment management fee that may be charged for this composite. For accounts calculated with a per share, net-of fee NAV, gross performance was calculated by adding back the unitary fee associated with that fund. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The investment management fee schedule for the composite is 0.39%; however, actual investment advisory fees incurred by clients may vary.

The U.S. Fundamental Stability & Value composite seeks to distill a starting universe of large cap U.S. equities into only the stocks where quality and value overlap using Distillate's proprietary definitions. Its goal is to achieve superior compounded long-term returns by limiting downside in periods of market stress, while still providing strong performance in up markets. This composite was created in May 2017.

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Free Cash Flow *refers to a company's operating cash flow, less its capital expenditures.*

Enterprise Value *refers to a company's market capitalization plus its net debt balance.*

Free Cash Flow to Enterprise Value Yield *refers to a company's or group of companies' free cash flow divided by the company's (or companies') Enterprise Value, with a higher resulting ratio indicating a more attractive valuation.*

Normalized Free Cash Yield (or Distilled Cash Yield) *refers to the firm's proprietary valuation measure that looks at estimated, adjusted free cash flow relative to a company's adjusted enterprise value. References to historical stocks that ranked well using this methodology refer only to these stocks' historical valuation and not their inclusion in any actual or hypothetical strategies/accounts managed by Distillate Capital Partners LLC.*

Long-term Fundamental Stability *is Distillate Capital's proprietary measure of through-cycle cash flow stability with a higher value indicating greater stability.*

Methodology note for Figures 6, 7, 8, 9 & 12: *free cash flow (FCF) figures reflect consensus estimates of next-twelve-months (NTM) FCF in comparison to enterprise value (EV) for the relevant portfolio/strategy or benchmark. Stocks without data are excluded and portfolios are reweighted accordingly. Stocks with FCF/EV values of greater than 50% or less than -20% have been eliminated to avoid distorting overall averages.* ***For Figure 7:*** *Cheapest third grouping is equal weighted.* ***For Figures 13 & 14:*** *stocks without data are excluded and portfolios are reweighted accordingly and stocks with leverage values of greater than 20 or less than -5 have been eliminated to avoid distorting overall averages. All data is as of 1/14/2022.*

The ***S&P 500 Index*** *is an index of roughly the largest 500 U.S. listed stocks maintained by Standard & Poor's. The* ***iShares Russell 1000 Value ETF*** *is an investable benchmark used as a proxy for its underlying index, the* ***Russell 1000 Value Index****, an index of U.S. listed stocks that possess attractive valuation as measured FTSE Russell. The* ***iShares MSCI ACWI Ex-US ETF*** *is an investable benchmark used as a proxy for its underlying index, the* ***MSCI ACWI ex USA Index****, an index managed by MSCI representing large and mid cap stocks outside of the U.S. The* ***iShares Russell 2000 ETF and iShares Russell 2000 Value ETF*** *are investable benchmarks used as a proxies for the underlying indexes of the* ***Russell 2000 Index*** *(an index of U.S. listed small cap stocks) and the* ***Russell 2000 Value Index*** *(an index of U.S. listed small cap stocks that possess attractive valuation as measured FTSE Russell).*

Indices are not available for direct investment. Investment in a security or strategy designed to replicate the performance of an index will incur expenses, such as management fees and transaction costs, which would reduce returns.

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Published January 16, 2022