April 14, 2022

Dear Partners,

Performance and Positioning Review – Q1 2022

Through Q1 2022, McIntyre Partnerships returned approx. 1% gross and 1% net. This compares to S&P 500 and Russell 2000 Value returns including dividends of -5% and -2%, respectively. Our investment in GTX/GTXAP is a "big bet" investment, which, given our concentration, makes market comparisons less useful at present. Since 2017 inception, the fund has returned ~19% gross.

Q1 2022 was one of the more volatile macro periods of my career. Typically, in a market correction, there is one large issue driving trading, such as COVID-19 in 2020 or the Greek Debt Crisis in 2010 and 2011. This year, there are at least four major issues impacting equities: the Russia-Ukraine war and its impact on commodities, rising interest rates, the bust of numerous highly priced tech companies, and the Chinese COVID lockdowns. The first few weeks of the year were primarily driven by the tech bust, and the fund was relatively inactive, as most of the carnage was in richly valued, yet often cash-burning companies I typically avoid. However, the Russian invasion triggered a more broad-based correction, and I have become more active. For now, our portfolio remains largely the same, but I have found a few new ideas which may become larger holdings.

Regarding the macro impact on our companies' fundamentals, automotive production is by far our largest look-through industry exposure. In my opinion, the deteriorating macro environment is a headwind to 2022 results but does not derail my long-term thesis. While global auto production is not immune from the impact of rising rates and commodity prices, the largest issue has not been weak demand but rather supply chain constraints, specifically semiconductors. Entering the year, I assumed the semiconductor bottleneck would improve by H2 and forecast volumes increasing 10-20% with a further recovery in 2023. Given the headwinds from the Ukraine war and China's recurring lockdowns, this now appears optimistic. I now think a 5% increase seems more realistic, with a larger rebound pushed out to H1 2023. However, this does not change my long-term view. One way or another, I am confident that global semiconductor capacity will eventually catch up with demand and auto production remains at severely depressed levels. The current auto downturn is now the largest since WWII and the vast majority of missing sales represent deferred rather than destroyed demand. Once the semiconductor issues are remedied, I believe global auto production will have a long period of strong gains, even if rising rates and inflation cause a small recession. Finally, and most importantly, GTX and CC trade at large current FCF yields even in this trough environment. Given their active share buybacks, we are benefiting from capital returns while waiting for global production to normalize.

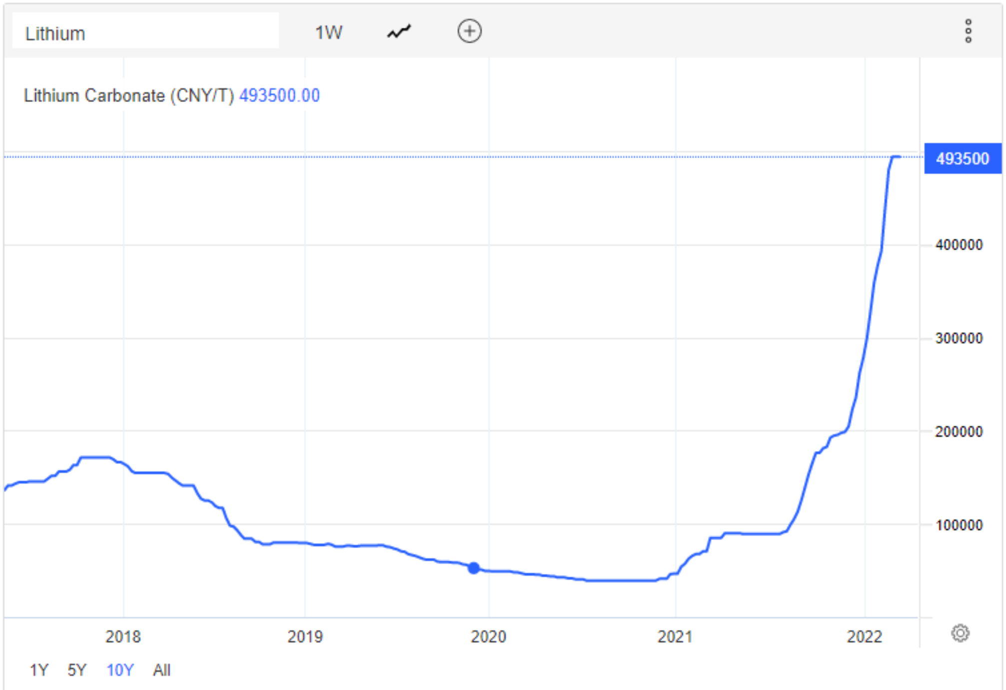
In the YTD winners' column, MSGE, VAL, and our China Tech basket contributed 100-500bps each. In the losers' column, GTX/GTXAP and CC lost 100-500bps each.

Portfolio Review – Exposures and Concentration

At quarter end, our exposures are 101% long, 0% short, and 101% net. Our five largest positions are GTX/GTXAP, MSGE, CC, our China Tech basket, and Permanent Bank, and account for roughly 89% of assets.

Portfolio Review – Existing Positions

Garrett Motion (GTX/GTXAP)



As I have written before, I believe battery electric vehicles (BEVs) are the future of auto, at least in certain parts of the world, and their growth is a direct threat to GTX's business. However, we are early to the disintermediation and BEVs currently account for only ~5% of total cars produced. With the stock at 3-4x FCF and competent capital allocators in control, I believe GTX's valuation is simply too cheap for BEVs to materially derail our investment unless BEVs show truly explosive near-term growth. At current prices, it does not matter whether BEV penetration is 20% or 40% in 2030; it matters whether it is 40% in 2026. On this front, I believe the YTD rally in lithium and cobalt prices strongly confirms my thesis that BEV penetration will take longer than GTX bears fear.

There are numerous headaches to BEV adoption, including range anxiety, lack of charging infrastructure, and BEV price tag, but I believe one could be a bull on all those points yet still run into the largest gating factor stopping near-term BEV growth: the lack of raw materials for batteries. BEVs require significantly more of certain materials, such as lithium and cobalt, than internal combustion engines (ICE), and there simply is not enough material available to hit aggressive targets in the next few years. Look at the charts above for cobalt and lithium – even before Russia's invasion, prices were soaring. For BEVs to be an issue for GTX in next 3-4 years, it would require lithium and cobalt supplies to increase fivefold, while simultaneously lithium and cobalt prices fall 90% to stimulate low-end car demand. Does that seem reasonable based on those charts? This is mining, not software, and you cannot build a railroad or dredge a port overnight. If BEV penetration is not above ~40% by 2026, GTX will generate its entire market cap in cash before the business even enters secular decline.

Longer term, roughly one third of GTX's sales and closer to 40% of EBITDA are commercial vehicles and aftermarket parts, which will not see a BEV impact for at least 10 years. I believe BEV penetration is likely to plateau at 60-70% sometime in the late 2030s, and there are many markets and use cases where I think a hybrid ICE using a GTX turbocharger will be used for years to come. For instance, Poland is 100% powered by coal, and until it switches to renewables, there is no point in BEVs as hybrid ICEs are more CO_2 efficient when coal is used to power the grid. GTX is also spending ~$100MM/yr. on R&D for products other than turbos, which over time could lead to products featured in BEVs.

<u>Portfolio Review – New Positions</u>

Interest Rate Hedges

In general, I do not hedge the portfolio for macro reasons and instead attempt to buy stocks with a margin of safety large enough to overcome macro issues. Having said that, regardless of stock selection, we are long a portfolio of yielding assets and are thus inherently taking interest rate risk. We can debate what is "priced in" to our various holdings, but rising rates do not benefit us on an absolute basis. My current worry is that inflation is running at a level that implies substantially higher interest rates than the market is currently pricing. Using the Taylor rule and the Fed's current assumptions, something like 6-8% would be an appropriate Fed funds rate while the market believes rates will be beneath 3% indefinitely. I honestly do not have a strong opinion on whether or not inflation will prove transitory, but I am reasonably confident that if a year from now inflation is still running at 8%, the market will be worried that rates must head higher and there are certain assets not priced appropriately for materially higher rates.

Rather than delve into the specifics of our hedge, I want to lay out the strategy. First off, I fully expect to lose 100% on our hedge and, as such, I plan to keep our gross investment small. Second, I am targeting deeply out of the money puts on assets with implied volatility lower than the S&P 500 Index, which should give the hedge a strong skew. Third, my goal is to lessen the blow of an interest rate shock, not generate overall positive PNL. If the market drops 30%, I fully expect the fund to be down, just less than otherwise.

As always, please feel free to contact me with any questions.

Sincerely,

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(1) The Returns from January through August 2017 represent the performance results of a personal proprietary trading account managed by the Founder with a strategy similar to the strategy of the Fund. This information is presented for illustrative purposes only, the above results do not reflect the actual results of the Fund or the composition of its portfolio. From September 2017 onwards, returns are from the Fund. All net returns are calculated using a 1.5% management fee, 20% incentive fee, and 5% hard hurdle.

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