McIntyre Partnerships

January 24, 2024

Dear Partners,

McIntyre Partnerships Quarterly Returns [1]

	Q1	Q2	Q3	Q4	FY GROSS	FY NET	RUSSELL 2000 VALUE
2017	25.9%	5.6%	11.7%	1.7%	46.1%	36.7%	7.7%
2018	-3.1%	3.2%	5.3%	-23.3%	-19.9%	-21.1%	-12.9%
2019	13.7%	-5.9%	-15.9%	8.1%	-2.9%	-4.4%	22.2%
2020	-55.9%	60.1%	28.5%	34.6%	21.8%	19.9%	4.5%
2021	32.5%	36.9%	-5.1%	5.5%	80.7%	66.0%	28.3%
2022	1.0%	-5.7%	-11.4%	19.6%	0.3%	-1.2%	-14.5%
2023	34.8%	0.7%	-6.5%	16.6%	48.2%	38.2%	14.7%
ANNUALIZED RETURN SINCE INCEPTION					*20.6%*	*15.9%*	*6.1%*
CUMULATIVE RETURN SINCE INCEPTION					*271.8%*	*180.2%*	*51.3%*

Performance and Positioning Review – FY 2023

Through YE 2023, McIntyre Partnerships returns were approx. 48% gross and 38% net. This compares to the Russell 2000 Value's return including dividends of 15%. This brings our five-year return CAGR to 21% net and returns since inception to 16% net versus 10% and 6% for the Russell 2000 Value.

In the winners column, record labels (UMG NA, WMG), GTX, our housing basket (FBIN, ZWS, FOR, MBC), and ALGN contributed 100-500bps, while SHC, MSGE/SPHR, and OSW contributed over 500bps. In the losers column, TPHS lost 100-500bps.

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2023 was a good year for the fund. However, it was not a particularly active one in terms of trading, and our top five holdings remained largely the same throughout the year. Instead, the seeds for our success were laid in 2022 when I substantially rotated the portfolio, and my 2023 adjustments were closer to pruning as various names over and underperformed throughout the year. Broadly speaking, I would bifurcate our returns into two buckets: a large gain in an idiosyncratic event driven idea (SHC) and broadly strong returns across the rest of our portfolio. I address the latter first.

Given our outperformance throughout 2022, I felt comfortable playing offense while most were playing defense, and I purchased several "baby with the bathwater" investments in high-quality businesses (OSW, record labels, our housing basket) that I felt were down due to the prevailing negative market sentiment rather than any long-term fundamental issues. As this negative sentiment reversed and the long-term earnings power of these businesses remained intact, their shares rallied strongly along with the broader market. While these investments outperformed the market, I believe several remain predictable, high-quality companies where a mixture of growth and proper capital allocation can still drive outsized results. As such, I am not in a particular rush to rotate our capital unless a compelling replacement can be found. However, I did exit our housing basket. In my opinion, the residential construction cycle is too volatile for us to own without a near to medium-term view of the housing cycle and/or exceptionally cheap valuations, which I neither have nor believe is present.

In addition, two long-held investments, GTX and MSGE/SPHR, had positive news during the year and were significant contributors to our overall gains. GTX announced a substantial one-time preferred dividend along with the conversion of the preferred shares, which we primarily owned, while simultaneously repurchasing roughly a quarter of the overall shares outstanding from the controlling shareholders. I view both events favorably and discuss GTX later in the letter. We retain a large position. For MSGE/SPHR, the split of the two businesses proved to be a significant catalyst, with the combined company rallying ~75% last year. After the spin in the spring, I rotated the bulk of our investment from MSGE to SPHR, as I thought MSGE was trading at a reasonable valuation while SPHR remained deeply discounted. Since then, SPHR has completed construction of the Las Vegas Sphere, which opened to broadly positive reviews, and SPHR has appreciated further. However, we have substantially reduced our investment in SPHR. I was comfortable owning MSGE in significant size due to its unlevered ownership of the Madison Square Garden arena, an iconic venue with stable cash flows and modest growth. After the split, SPHR has no ownership of the arena and is instead a riskier growth company, with significant upside potential but also higher odds of a miss. As a result, we retain a smaller position in SPHR. Looking forward, I remain bullish on the Las Vegas Sphere and believe additional sphere developments could be a significant catalyst, offset somewhat by my worries regarding refinancing the MSGN loan while SPHR is still bearing a great number of front-end loaded growth expenses.

The notable outlier to our "generally good" overall portfolio was SHC, where the settlement I was expecting drove shares up by over 100% in January 2023. In response to the outsized move, I reduced the position by roughly half. After its January surge, SHC's shares have largely been range-bound. Despite the significant gain and lackluster performance since, I believe SHC remains a compelling investment. It is the fund's largest position, and I go into greater depth below.

Finally, regarding new investments, I identified and bought several small investments during the H2 market selloff. However, as the market recovered, their shares ran with the market before we could build a significant position in any. We maintain a number of these smaller positions and I could see rotating significantly at some point. For now, I am sitting tight, continuing to look for new ideas, and seeing if anything interesting shakes free.

Portfolio Review – Exposures and Concentration

At quarter end, our exposures are 102% long, 6% short, and 96% net. Our five largest positions are SHC, OSW, GTX, record labels, and STHO/SAFE, and account for roughly 80% of assets.

Portfolio Review – Existing Positions

Sotera Health Company (SHC)

In a vacuum, SHC screens as my ideal type of business: one half of a duopoly market with good long-term growth where the product sold is mission critical to customers, with high switching costs, yet the product's cost is immaterial to their customers. In the case of SHC, the company is one of two scaled outsourced providers of medical device and pharmaceutical sterilization services. SHC is diversified across almost all major medical device and pharmaceutical manufacturers, boasts a 100% retention rate with top customers, and has consistently grown sales at close to 10%. Further, sterilization represents ~1% of their customers' cost of goods sold, and SHC has an ~55% EBITDA margin. Normally, a consistent 10% growth story with 55% margins would trade at a significant multiple. Indeed, from when SHC IPOed in late 2020 until legal fears derailed the stock in fall 2022, shares consistently traded over 18x EV/EBITDA and 25x P/E, yet shares currently trade less than 12x my 2024 EV/EBITDA and 15x my 2024 EPS.

I believe a trifecta of headwinds has held SHC back since the settlement. Importantly, I believe those headwinds will largely abate in the next year or two, and that SHC's multiple can normalize while the business continues to grow. First, SHC slightly missed expectations due to destocking at medical device manufacturers as global supply chains normalized, a phenomenon seen in many industries. I believe this is the largest issue holding SHC back and I expect it to be resolved this year. Second, med device stocks broadly fell last year due to fears surrounding GLP-1s' impact on obesity-related medical procedures. While SHC is correlated with med device stocks, I do not believe GLP-1s will materially impact SHC's volumes, as the risk is speculative, long-term in nature, and the "at risk" obesity-related portion of medical devices is under 5% of SHC's overall mix. Third, I believe many investors are still hesitant to invest in SHC in case the legal liabilities resurface. As partners know, I have invested in numerous companies with legal overhangs, but it is difficult for investors without relevant experience to believe the coast is clear, so to speak, even after the bulk of the storm has passed. This represents an opportunity to purchase shares in SHC at a discount despite its current litigation outlook being manageable and not too different from most companies' legal risks. A similar phenomenon has played out with our CC investment over the last five years. In 2019, a short seller simply pointing out that there was legal risk caused a 70% drop in the stock. In 2023, CC announced a massive settlement, followed by legal risks putting that settlement at risk, yet the stock did relatively little on the news in both directions. It takes time for people to digest litigation risk, and it is difficult to know precisely when they will. But eventually, they do, and I believe the normalization of SHC's multiple to levels seen before its collapse in fall 2022 represents a significant catalyst. I estimate SHC will earn $700MM in 2026 EBITDA and $1.50 in 2026 EPS. 18x EV/EBITDA and 25x P/E yields $37 versus the current share price of $15.

Garrett Motion (GTX)

I have written on GTX many times previously, and I will not bore partners with a rehash. Instead, I want to focus on the significant slowdown in battery electric vehicles (BEV) growth.

Units (MMs)	**2021**	**2022**	**2023e**	**2024e**	**2025e**	**2030e**
North America	0.5	0.8	1.2	1.8	2.6	9.0
Europe	1.3	1.7	2.1	2.4	3.2	10.1
China	2.4	4.2	5.2	6.3	7.5	15.4
ROW	0.4	1.0	1.3	1.5	2.0	7.6
Global	**4.7**	**7.8**	**9.8**	**12.0**	**15.4**	**42.1**
y/y % growth						
North America	75%	61%	48%	48%	44%	
Europe	66%	28%	25%	15%	34%	
China	169%	74%	22%	22%	19%	
Global	112%	65%	**26%**	**23%**	**28%**	
Penetration Rate						
North America	3%	5%	7%	9%	13%	45%
Europe	10%	13%	15%	17%	21%	60%
China	12%	21%	24%	28%	32%	60%
Global	**6%**	**10%**	**11%**	**14%**	**17%**	**45%**

Source: Wolfe's BEV Growth Forecast

The slowdown I have long predicted is materializing, and I believe the "stronger for longer" tail of internal combustion engines (ICE) and hybrid power trains, which account for ~60% of the company's EBITDA, has materially increased in value. Despite this, GTX currently trades ~5x my 2024 FCF and I believe GTX will return at least half to shareholders via buybacks. Simply put, I believe the slowdown in BEV is heading on a collision course with GTX's valuation and proper capital allocation. Without a significant reacceleration in BEV sales, it is difficult to see how GTX will not be a significant winner eventually. However, rather than rehash all the puts and takes of the bull versus bear debate, I want to update our risk/reward framework over the next three years.

To the downside, if BEV unit growth reaccelerates towards a mid-30s growth rate, I believe GTX's EBITDA could be roughly flat in 2027 as continued share gains in existing ICE and hybrid powertrains and a modest cyclical recovery offset the mix lost to BEVs. Importantly, I believe GTX would generate roughly $1.2B in FCF in that time, with half going to buybacks and half to debt paydown. Depending upon assumptions for what price the shares are repurchased, a punitive 4x EV/(EBITDA-capex) multiple would yield a stock price roughly flat to up slightly from current levels.

To the upside, if BEVs were to continue decelerating, I estimate GTX's 2027 EBITDA could be 25% larger than at present and EPS could reach $3. Further, in a world where BEV penetration is plateauing, hybrid powertrains requiring GTX's state-of-the-art turbos would play a critical role in decarbonizing transportation. For instance, MIT estimates the savings from switching from internal combustion to hybrid results in a ~50% reduction in CO2 versus a 65% reduction from BEVs. If GTX were to trade 12x earnings, roughly the standard auto supplier multiple before the 2020 recession, shares would trade $36 versus $9 today.

While I am acutely aware government mandates, continued BEV innovation, and falling battery prices could boost BEV demand, I believe GTX is an opportunity where we stand to lose little if wrong while making a great deal if proven right.

<u>Business Updates</u>

Our team grew notably in 2023 with Briana Barnhart joining us as our administrative assistant, EAC as our CFO/COO, and Pillar as compliance. Thankfully, their efforts are already benefiting our operations and I am grateful for their hard work and happy they are on our team. We plan to distribute K1s in the coming weeks.

Two more notes. I will be attending iConnections in Miami next week and I would love to see any partners or potential ones who may be in town. I have also been engaged with and am currently exploring accelerator transactions to help our firm grow. If anyone is interested in participating in such a transaction, I would welcome the conversation.

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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