FIRST QUARTER 2020 LETTER

For the first quarter of 2020, the Ballast Portfolio returned -33.4% before fees and -33.6% net of fees, compared to -34.6% for the Russell 2500 Value and -29.7% for the Russell 2500.

		Periodic Returns						Annualized Returns	
		2015*	2016	2017	2018	2019	1Q 2020	1 Year	3 Year
Ballast Portfolio[1]	Gross	-7.6%	23.8%	13.5%	-2.2%	16.1%	-33.4%	-30.7%	-5.6%
	Net	-8.0%	22.6%	12.4%	-3.2%	15.0%	-33.6%	-31.4%	-6.5%
Russell 2500 Value[2]		-5.8%	25.2%	10.3%	-12.4%	23.5%	-34.6%	-28.6%	-8.4%
Russell 2500		-6.9%	17.6%	16.8%	-10.0%	27.7%	-29.7%	-22.5%	-3.1%

Performance (as of 3.31.2020)

*2015 performance from 8.11.2015 through 12.31.2015

KEY POINTS

- Although the greater than 40% drawdown in R2500 has been painful, and while there may be another leg down, we are amidst a once-in-a-decade buying opportunity.
- We used the drawdown to take 13 new positions, following our standard discipline of investing in companies with strong balance sheets, ample liquidity to survive a long recession, identifiable competitive advantages or cost leadership, and ample upside in a recovery.
- Although scary, now is the time to invest in small caps. The Federal Reserve's $4.5 trillion indicates asset inflation of 20%-40% in equities, and small caps have outperformed large caps by an average of 18%-20% over the one and two years following a bottom.
- A recession started in April, and new US cases of COVID-19 appear to have peaked. In other regards, the future is unusually uncertain. We will get through all of this.
- Our returns did not hold up as well as we would have hoped in 1Q20, but we still expect controlling risk at a fundamental level will result in lower downside capture when measured over periods longer than a quarter. Moreover, upside is more than intact – our estimated reward-to-risk ratio for the portfolio is 6:1.

Dear Fellow Investors,

Foremost, we hope that you and your family members and colleagues continue to be safe and healthy as we continue to manage through these unprecedented and challenging times.

We have a lot to say this quarter. We will hit on how we are approaching the unusually uncertain future, how QE will drive stocks, how small caps outperform off the bottom, our career record 13 new positions initiated in two months, and last quarter's performance. But first, a brief anecdote of obvious relevance.

Courage is being scared to death but saddling up anyway. – John Wayne

I was eight the first time I got bucked off a horse. I was casually riding around the pasture when my dad decided to feed the other horses. (Finally, a story where he is the knucklehead!) My horse saw the others getting fed, and decided I was a nuisance. I did a somersault on the way down, landed hard, and I had absolutely no intention of getting on a horse ever again. Dad, of course, would have none of that. Getting back in that saddle is one of the first life lessons I can recall. Life is often hard and sometimes dangerous. When you get bucked off a horse, you stand up, dust yourself off, and climb right back on. The global financial markets just took one heck of a fall, as did we. In pain and a little fearful, we are dusting ourselves off, climbing back in the saddle, and ready to ride.

Yomping into uncertainty

Markets and news have driven a fast and furious rollercoaster, which we expect will continue awhile, so we are sticking tight to our standard processes and disciplines, preparing for the recovery while seeking to limit downside. Limiting downside is particularly important at the moment. At a macro level, there are more than a few moving pieces to consider including but not limited to: COVID-19, social distancing, infinite QE, surging unemployment, forecasts of double-digit GDP declines, record fiscal deficits, trade wars and, let's not forget, both political parties all aboard with sending checks to low-income households.

We have built a parsimonious model to forecast the peak and course of COVID-19, but it does not include the complex political variables nor the impact on GDP. We do not want to pretend to make sense of it all, so we will not share the details unless you ask. That said, we believe social distancing has brought the rate of transmission down enough to say that the peak rate of infection is behind us.

We can say with far more certainty that the recession has already started. Using jobless claims to forecast the unemployment rate, then applying the Sahm rule, clearly puts the start of the recession in the first week of April – with obvious ramifications for corporate outlooks this year. (The Sahm rule states that a recession has begun when the trailing three-month average of the unemployment rate is more than 50bp higher than the lowest unemployment rate in the last 12 months.)

Offsetting the dire implications of COVID-19 for the economy and corporate earnings, the Federal government has enacted $6.5 trillion of stimulus and QE, with the promise of more to come. Some will argue that valuations are too high for a bull market to start, especially since bottom-up estimates almost certainly will reset lower as economic and earnings news gets ugly during the 1Q20 earnings season. There may be another leg down as this news hits, but it is so well anticipated in a general sense that it is far from certain equities will follow. In a crisis, timeframes contract, and the next six months of earnings are likely to be ugly. But as this crisis passes and clarity builds, horizons will lengthen again to focus on earnings power and, as important, real returns.

The total $6.5 trillion is equivalent to roughly a third of a year's GDP. What happens when countries debase their currencies? After Nixon ended the gold standard in August 1971, stocks rallied 7% in the following three weeks and ended 1972 up 25%.

It is harder to know whether this will lead to general price inflation. While globalization pressures may dissipate as companies seek to diversify and shorten supply chains, the technological forces keeping wages under pressure are persistent. Either way, real assets, including equities, are likely to be increasingly important to institutional investors, especially as the diversification benefit of long-term fixed-income evaporates at the lower bound. Let us not forget that the negative correlation with stocks is an artifact of falling interest rates, that before the 1980s stocks and bonds went up and down together. Are treasuries worth it without the negative correlation? Presumably, equities will have to do more of the heavy lifting.

By whatever name, Quantitative Easing drives asset inflation

The Federal Reserve, for its part, has promised $4.5 trillion of liquidity, roughly equal to all the prior rounds of QE combined. For the last decade, we have seen no evidence that QE leads to general inflation, only asset price inflation. That the opposite is also the case, quantitative tightening leads to asset deflation as in the 2018 taper tantrum, provides further evidence in support of this model. The following table shows that during periods of QE, the S&P 500 advanced at an average 18% CAGR, corresponding to the Fed balance sheet increasing at a 45% CAGR. That implies each 250-basis point (bp) of balance sheet expansion corresponds to 100bp of QE upside. In non-QE periods, the S&P's CAGR was 5%, and the Fed's balance sheet was -1%.

				Total Change		CAGR	
Period	**From**	**To**	**Days**	**SPX**	**Fed Assets**	**SPX**	**Fed Assets**
QE1	8/29/2008	3/26/2010	574	-9%	154%	-6%	81%
Non-QE	3/26/2010	10/29/2010	217	2%	-1%	3%	-1%
QE2	10/29/2010	7/1/2011	245	13%	25%	20%	39%
Non-QE	7/1/2011	10/26/2012	483	6%	-1%	4%	-1%
QE3	10/26/2012	12/27/2013	427	30%	42%	25%	35%
Non-QE	12/27/2013	9/6/2019	2079	62%	-7%	9%	-1%
Stealth QE	9/6/2019	2/14/2020	161	13%	11%	33%	27%
				QE Periods Average		18%	46%
				Non-QE Periods Average		5%	-1%
				Full Period		8.8%	14.2%

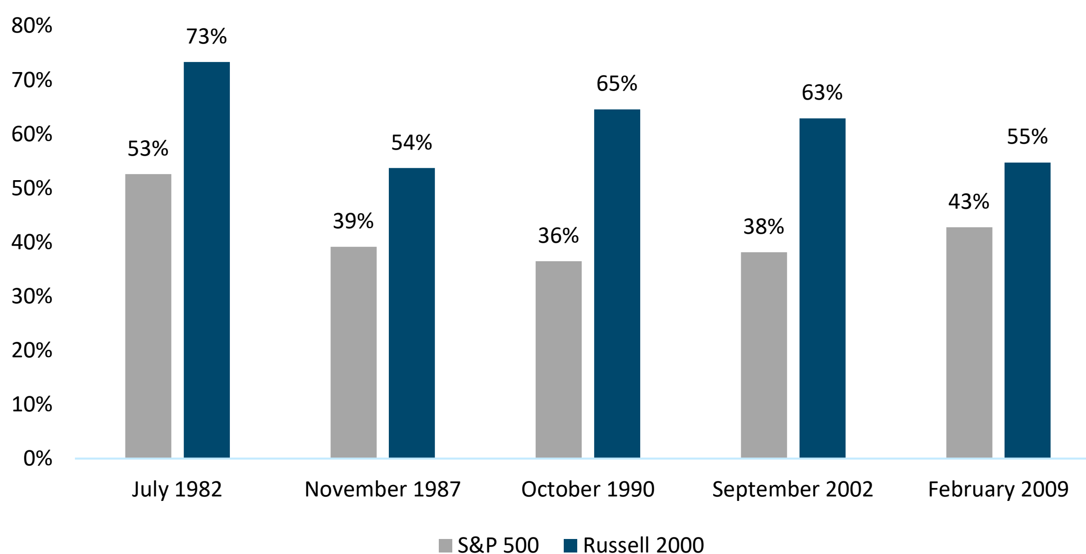
Since reacting to the COVID-19 liquidity crisis, the Fed balance sheet is currently up $1.9 trillion or 30%, while the S&P is up 22% from the bottom. With the Fed's balance sheet set to grow another 50%, there is still **at least another 20% QE-driven upside**. If we include the Fed's response to COVID-19 so far in our baseline, then each 160bp increase in the balance sheet delivers 100bp of SPX appreciation. That implies an additional upside of about 30% from QE. If we assume that QE1 did have an impact on equities but exclude it because we cannot measure it in the contemporaneous period, then 100bp of Fed balance sheet expansion drives 70bp of S&P 500 increase, roughly **40% of asset price inflation**.

We refer to QE upside because, as we saw in 2008-9, real economic events can swamp the effect of QE in the immediate timeframe. We give that due consideration as we navigate the current environment, since, in contrast to the housing bust, the financial crisis came before the real economic crisis. As with any model, we cannot rely on it with too much confidence. However, we are confident that the earnings season is going to be quite interesting this quarter.

Big returns in small stocks

Following market troughs, small caps have outperformed large caps by 19%, 18% and 20% over the 12-, 18- and 24-month timeframes.[1] Financially sound small and midcap stocks appreciate faster for at least two fundamental reasons. First, they can typically navigate more efficiently and be better positioned to lead than large companies when entering a recovery. Second, they tend to be less sensitive to interest rates and other economic factors, which we believe will afford them with a clearer path to grow and increase in value.

[1] Analysis was based on 5 drawdowns of greater than 15% in the S&P 500 since 1980. Monthly data was analyzed and S&P 500 trough dates included 7/30/1982, 11/30/1987, 10/31/1990, 9/30/2002, and 2/27/2009. Small cap outperformance was measured by averaging the difference in non-annualized index price returns of the Russell 2000 index relative to the S&P 500 Index over the respective timeframes following the S&P 500 trough date.



Trough date based on S&P 500 Index. Subsequent returns non-annualized, based on index price change.
Source: Bloomberg

History rhymes, but do not get too cute

The market, economic and personal uncertainties are palpable, but now is the time to start buying. Waiting for signs of the recovery means missing one of the most meaningful parts of the investment cycle – the returns off the bottom that typically occur in short sharp moves in small windows – if you are not ahead if it, you miss it. Timing market and stock bottoms to the day or even week is a mug's game; we believe it is best to be early, with fundamental risk control. In general, stocks tend to rally about six months in advance of actual recovery. If the economic impact of COVID-19 is only a two-quarter hit to GDP, we have probably seen the lows. If it is a more prolonged recession, there could be another leg down with earnings, but that will hopefully be fine-tuning as opposed to indiscriminate, forced selling.

It is important to remember that households are in far better balance sheet shape than at the start of the Great Financial Crisis (GFC) and that housing today is undersupplied versus oversupplied then. When the $2.1 trillion of fiscal stimulus hits the economy, with the promise of more to come, we believe it is going to dwarf the Trump Tax cut and power the economy out of whatever slump COVID-19 causes. There will be winners and losers, but direct payments to lower-income consumers should prime the pump much quicker than the trickle-down wealth effect of QE, leading economic activity to pick up more quickly and creating new opportunities for those displaced by COVID-19.

Although the financial crisis is likely contained, fundamental risk remains, including:

- COVID-19 spiking again before more judicious responses have been formulated, potentially requiring a second round of ham-fisted social distancing and putting a pause on the economy's ability to restart.
- How long social distancing lasts is a function of how long it takes to mobilize the resources to handle future COVID-19 outbreaks with greater finesse, and the rate prevention measures can be put in place (i.e., testing).
- Fiscal and monetary policy fails to adequately propagate to smaller businesses, leading to a ripple effect of failures that cost jobs and stop people from getting back to work quickly, in which case the sharp recession underway risks dragging into something worse.
- Further stimulus does not materialize. In the two-quarter scenario, this is less of a problem for the market than for individual stocks that stood to benefit from infrastructure initiatives. If the recession lasts three quarters, and further stimulus is not enacted, there is a higher risk of an L-shaped recovery.

Each of these risks suggests that any levered companies need to have ample liquidity, loose covenants, and no significant debt maturing before 2022.

Portfolio Changes

Although we have been working from home, we are working harder than ever to capitalize on the indiscriminate selling last month, to sort great opportunities from the general wreckage. We added 13 new positions in Q1 and the first couple weeks of April, while increasing positions in others already held. These stocks fall into three buckets:

1. Extremely high-quality companies with sustainable competitive advantages that usually trade at extremely high valuations, but not at the moment. For instance, we took new positions in Capital Bancorp (CBNK), Landstar (LSTR), Lennox (LII), MGE Energy (MGEE), Silicon Valley Bank (SIVB), and J&J Snack Foods (JJSF).

2. Good businesses with solid secular prospects unreasonably caught up in the forced and panic selling, the proverbial babies thrown out with the bathwater. Examples include Lumentum (LITE), Cerence (CRNC), Iradimed (IRMD).

3. Stocks with severely depressed valuations (usually with some leverage) where our analysis shows the companies can survive, regardless of the length and severity of the virus-induced recession, and have significant cyclical upside. These stocks include Essent Group (ESNT), NRG Energy (NRG), Farmer Mac (AGM), Pulte Homes (PHM).

New Positions Initiated

Capital Bancorp (CBNK) is a small but high-quality regional bank based in Maryland and serving Washington, DC. It earns a premium net interest margin by offering high-touch, consultative solutions to smaller and medium-sized businesses. Insiders own about 42% of the equity and constitute approximately 10% of the deposit base, which reinforces a very strong credit culture. The loan book is mostly composed of construction and commercial real estate loans, principally multifamily housing, with less than 10% tied to retail and restaurant or similarly vulnerable end markets. It also owns a national mortgage origination platform and a secured credit card business aimed at consumers looking to build or rebuild credit scores. Both businesses are fully digital. The savings accounts securing the credit cards account for approximately 20% of deposits and are growing low double digits. The bank earns 12%-13% ROE, with potential upside as digital and human fixed costs leverage. At purchase, it traded at about 1.0x BVPS versus its normal 1.5x-1.6x range.

Cerence (CRNC) is an auto-focused voice recognition software company that spun out from Nuance Communications (NUAN) last September. The company enjoys several long-term secular growth trends related to increasing sophistication and penetration of connected technology features in vehicles. While cautious about the near-term outlook for global auto sales, especially in China, we initiated a position in February. The stock held up very well in March, perhaps indicating the market is willing to look through the near-term disruption in auto production to the attractive long-term prospects. We will look to increase the position after confirmation that business disruption is behind them or attractive reward-to-risk.

Essent Group (ESNT) offers private mortgage insurance (PMI) on residential property loans, similar to another current holding, MGIC Investment Corp (MTG). We initiated a position in Essent to increase our exposure to this undervalued sector. Relative to its peers, Essent has the strongest credit profile and best fixed charge coverage ratio, while offering strong growth and industry-leading returns on equity.

Farmer Mac (AGM) is a federally chartered secondary buyer of bank loans made to the agricultural industry. They generate returns on equity of 18% and grow earnings at about 10% per year. The stock sold off and traded at 7x earnings with a 5% dividend yield. Unlike its cousins, Freddie Mac/Fannie Mae, Farmer Mac is differentiated by the following: 1) the loan-to-value is substantially lower, around 50% for Farmer Mac compared to more than 95% for Freddie/Fannie in the crisis, and 2) the government directly supports farmers' income through subsidies, the programs for which will likely be protected by bipartisan political support in the future.

IRadimed (IRMD) is a medical device company that supplies non-ferrous IV pumps and monitors to hospitals for safe use within the strong magnetic fields of MRI scanners. The company enjoys market leadership, high returns and margins, a long runway for growth, and exciting new product development prospects that leverage its existing salesforce focused on hospital radiology and intensive care unit

departments. We initiated our position earlier in the quarter and bought more after substantial market declines. While their near-term revenues will likely be materially impacted by the absence of elective procedures at hospitals during the shutdown, we expect that IRadimed's competitive position supplying a differentiated and medically necessary device will be maintained. That and their net cash balance sheet should protect them from financial distress.

J & J Snack Foods (JJSF) is a company we have followed for many years, waiting for a great buying opportunity like the one we saw this quarter. The high returns and long runway make it a company that can compound value over a long period of time. However, like many other great businesses, the COVID-19 response hit their sales in an unexpected and severe way. We believe it is likely that sales of their concession foods sold at stadiums and malls go to zero in the near term, leaving a huge gap in their revenue for the year. However, with a strong balance sheet, we believe they will emerge from this downturn fully intact and that they will continue to compound returns going forward.

Landstar (LSTR) is an asset-light trucking company with low fixed costs, minimal capital requirements, mid-30s returns on equity, and a net cash balance sheet. It has been a wish-list stock and one we have owned in the past. Landstar is unique in that it sources loads through independent commissioned salespeople. Business Capacity Owners (BCOs) enter exclusive contractor relationships at either contracted or per load rates, and those BCOs own and operate their own trucks. Landstar uses its scale to negotiate discounts for BCOs on things like tractors, tires, fuel, repairs, and insurance. They lead a stable workforce of independent businesspeople, all incented to be as efficient as possible. We initiated a position consistent with our aim to high-grade into great businesses during the drawdown. Further, Landstar's role with independent truckers providing essential logistics services should insulate to some extent from the shelter-in-place rules. Finally, it offers attractive upside leveraged to the economic recovery, and importantly, it does not require us to time that recovery because it maintains a healthy balance sheet and sustainable business model.

Lennox International (LII) is a high-quality HVAC/R business with mid-teens ROA, low- to mid-single-digit secular top-line growth driven by GDP and market share gains of 25bp/year, and solid capital allocation reinforced by ROIC component of management compensation. It's approximately 75% replacement demand mitigates the cyclicality of construction demand. New build indexes are approximately 60% residential which is a secular tailwind, 25% commercial and 15% refrigeration/EU. It underearned in 2019 due to the 2018 tornado and weather, and 2020 will still be a partial recovery year beyond the COVID-19 impact as it seeks to regain contractors that left due to tornado-related stock-outs. The impact of COVID-19 is not fully in 2020 consensus estimates and our expectation is about 20% lower. Although we expect estimates to come down, this is more than accounted for in recent multiple compression driven by the market-related drawdown, and we expect that within nine months the stock will trade on 2021 earnings power. We see upside optionality in store optimization, digitization, value engineering and pricing pushing operating margins above 20% over the next three years. Management targets net debt-

to-EBITDA of 2x, which is higher than we'd normally like, but this is offset by the stability of replacement demand and its strong competitive position as demonstrated by its 15%-20% ROA over the last five years.

Lumentum (LITE) is an optical and photonic laser provider to original equipment manufacturers (OEMs) and network equipment manufacturers (NEMs). The business has its origins in optical network leader JDS Uniphase but has since developed key businesses with strong secular growth tailwinds. First, they provide 3D sensing technology used on smartphones (including Apple) to provide real-time depth information to photos and videos (like facial recognition to log into the phone). Second, their laser technologies are used to support higher data rates demanded by the global implementation of 5G networks. We initiated a position in February and added more in March.

MGE Energy (MGE) was the second utility we bought in the quarter. MGE Energy, also known as Madison Gas & Electric, provides electricity generation and distribution and natural gas distribution to customers in Wisconsin. The company operates under one of the most favorable Public Utilities Commissions in the country (the PUCs set return targets regulated utilities are allowed to earn). During the sharp declines in March, MGE appeared to be on the wrong side of a forced seller, and we took advantage by buying the stock at attractive prices with a highly favorable reward-to-risk profile.

NRG Energy (NRG) is a vertically integrated, unregulated utility that generates an 11% return on assets, but was trading at a double-digit FCF yield and mid-single-digit dividend yield at the time of our initiation. Over the last five years, under the stewardship of a new returns-focused CEO, the company paid off $14 billion in debt and brought down net debt-to-EBITDA to 2.9x, within the company's long-term target range. Going forward, they plan to maintain the dividend and buyback stock (paying $295m in dividends and $440m or more for repurchases). NRG will deploy capital on growth projects achieving a 12%-15% unlevered hurdle over five years. If no projects meet those targets, they will buy back additional stock. We opportunistically added NRG to the portfolio, and as a stable business trading at a discount, we believe it offered a very attractive buying opportunity.

Pulte Homes (PHM) builds housing for first-time, move-up and mature homebuyers across most of the country. Scale and standardized building processes give it an advantage over small and local builders. Pulte is one of the largest homebuilders and yet has just 3% market share. Despite fragmentation, housing is inefficiently priced, homes are not commodities. It hasn't been this cheap on an asset basis since 2012. Last time PHM traded at this EV multiple of cash+inventory, the next 12-month return was ~100%. We were initially skeptical, but PHM is far more cash flow and ROIC focused than earlier in the century. Near term, homebuilding is designated as an essential business in many jurisdictions and PHM has 10.5k units in backlog, enough to stay busy for 5-6 months. (LTM closed 24k homes.) Longer term, housing is under-supplied, especially at low end. First-time buyers are 29% of PHM's mix and heading higher. It's earned very strong ROA of 9%-10% over the last couple years, and while that will likely dip this year, we believe it is sustainable long term. It has approximately five years of land inventory which, as it works down toward a target of 36 months, is a tailwind to cash flow. FCF was approximately $1b each of the last three

years, which together with $1.2b of cash on the balance sheet and roughly $730m of revolver capacity gives it ample liquidity to manage its total debt of $3.2b. It has no significant covenants and its next maturity is $426m due in 2021.

SVB Financial (SIVB), also known as Silicon Valley Bank, is a high-quality bank that has historically been too expensive for us. While not quite to historic low P/B, it traded at an attractive reward-to-risk, and we decided to swap the position for East West Bancorp (EWBC). To us, the most interesting aspect of SIVB is that they get warrants for a lot of tech company start-ups as a result of their relationships with those companies. Currently, they have warrants in over 2,000 companies, and these pay off big when these small companies grow up and become public.

Exited Positions

Alexander & Baldwin (ALEX) is a Hawaiian-focused REIT that holds land, retail, residential and commercial assets. The company's retail business was caught in the crosshairs of COVID-19. As retail tenants miss rent payments at unprecedented levels (only about 30% of retail tenants paid rent in April), Alexander & Baldwin's strip malls and high-end retail exposures pose a risk and uncertain timing related to recovery.

AMC Networks (AMCX) had several hit TV shows and huge free cash flow associated with that success. Still, the move from traditional pay-TV to app-based viewership, the entrance of behemoths Netflix/Amazon/Apple/Google into content production and subsequent price discounts have turned this industry upside down in the near-to-medium term. It is unclear at this point how this will all play out, so we sold the position and redeployed proceeds into better opportunities.

Criteo (CRTO) sold off previously on the effect of changes to Google's cookie policy for its widely used Chrome browser. Since Criteo's retargeting business depends on the ability to track users without using personally identifiable information (PII), cookies play a central role. While it is not clear yet exactly how the ecosystem develops, the changes violated our thesis because they may likely require some combination of substantial cap-ex spending, reduced bargaining power and/or increased competition. We sold the remaining position in January based on the thesis violation.

Designer Brands (DBI) came under unprecedented pressure due to COVID-19. First, supply chain disruption stemming from China's shutdown posed a substantial risk to domestic shoe buyers, particularly in the fashion/dress shoe segment. Second, they, like other retailers, were forced to shut stores, sending near-term revenues close to zero. While their balance sheet and digital store should help mitigate, the headwinds in the near term and the uncertainty on the timing of normalization in retail were too great. We chose to sell this position to fund better buying opportunities.

East West Bancorp (EWBC) is a high-quality bank and has been a long-term holding for us. We chose to sell the position to fund a swap into an even higher-quality bank, Silicon Valley, as both sold off significantly in March.

LogMeIn (LOGM) had previously announced plans to be acquired by private equity buyers. We sold half of the position, as is our standard operating procedure, upon the announcement. We sold the remainder early in this year before the dramatic sell-off and subsequent recovery in the stock price, as the go-shop period ended and the closing date approached.

Oshkosh (OSK) was a strong performer for us over multiple years. Fortunately, we previously sold into that strength and maintained a small position coming into the year. We sold the remainder in January after earnings missed expectations, and we saw an indication of the early cycle segments starting to decline. We noted that while the defense business continues to grow, we received an indication that the aerial work platform segment would likely continue to face headwinds throughout 2020. That assessment proved correct, as we were able to sell a very procyclical business ahead of the pending recession and stock price declines.

Orthofix (OFIX) violated our investment thesis when they announced a dramatic spending increase to accelerate future growth. Our thesis was they would be able to drive modest organic revenue growth and higher margins with the existing product set. While this acceleration bet may be a successful venture for the company, the results are at least a year out, bringing uncertainty about its success and its long-term profitability. We will revisit upon confirmation that increased R&D spending is actually leading to higher and, importantly, profitable growth.

Westrock (WRK) was an underlevered company in a consolidating industry when we initially invested. Our thesis was that industry consolidation and rationalization would bring about better price stability to the industry with fixed capacity and volatile demand. While that pricing stability thesis has largely played out, Westrock was the most aggressive acquirer and used debt to fund the acquisitions. At this point in the cycle, we were not comfortable with the level of debt. We sold the stock at the end of February, fortunately avoiding most of the drawdown in March.

Performance

February and March were by far the most violent period we have experienced in markets. Volatility shot up, and correlations spiked across asset classes (Equities, Fixed Income, Precious Metals). Our fundamental risk model did not contemplate a global pandemic, nor did our fundamental downside analysis consider revenue going to zero for a period of time. There will be plenty of time spent dissecting this in our future post-mortems, but now is a time for action. We are using all our collective research, analysis, experience and tools to actively invest and to position the portfolio for future capital appreciation while limiting risk.

1Q 2020 Top and Bottom Performance Contributors

Top Performing Positions			Bottom Performing Positions		
	Name	Total Return		Name	Total Return
LMNX	Luminex Corp	+19.3%	**CRMT**	America's Car-Mart	-48.6%
SIVB	SVB Financial	-6.7%	**SOI**	Solaris Oilfield	-61.7%
MGEE	MGE Energy	+2.6%	**CNXM**	CNX Midstream	-49.4%
JJSF	J & J Snack Foods	+4.8%	**CIT**	CIT Group	-61.9%
LOGM	LogMeIn Inc.	+0.3%	**NTIC**	Northern Technologies	-47.1%

Top 5 Contributors

Luminex (LMNX) is a diagnostics provider and is naturally well-positioned to respond to needs for COVID-19 testing. In early March, Luminex's CEO announced that they were working on solutions to test and diagnose the virus on their NxTAG and ARIES platforms. By the end of March, they had received emergency use authorization (EUA) by the FDA for the NxTAG coronavirus panel. After the quarter end, Luminex also received emergency use authorization for its targeted test, which runs on its ARIES system. The monthly production capacity for the panel and targeted tests are 300,000 and 200,000, respectively.

SVB Financial (SIVB), also known as Silicon Valley Bank, was added after selling East West Bank (EWBC), allowing to further high-grade the portfolio with a better position. While both are relatively high-quality banks, Silicon Valley was a unique opportunity in our view, as it historically trades at a premium price-to-book multiple. Part of what is unique about SVB Financial is their close relationships with tech start-ups. As a result of their client base, the bank owns warrants in over 2,000 innovative companies, offering upside optionality when those small start-up companies grow and reprice in subsequent offerings.

MGE Energy (MGEE), also known as Madison Gas & Electric, is a regulated utility with electricity generation and distribution and natural gas distribution to 140,000 commercial, residential and industrial customers in Wisconsin. While the business is very stable, the stock price in March was not. We took advantage of the opportunity and purchased shares in the utility at attractive reward-to-risk.

J&J Snack Foods (JJSF) was added in the quarter. While the company's concession snack foods will take a direct hit by the shelter-in-place, the sell-off created an attractive long-term buying opportunity. Bolstered by a strong balance sheet, the company's high returns and long-term growth prospects remain intact.

LogMeIn (LOGM) was completely sold from the portfolio in early January, prior to the onset of market volatility. As is our customary procedure, we had sold the first half of the position on the announcement of an agreement to be acquired by private equity buyers last year.

Bottom 5 Detractors

America's Car-Mart (CRMT) faced a steep decline as the shelter-in-place rules threaten new auto sales and expose them to higher consumer credit risk for its outstanding loans. We remain convinced, however, that America's Car-Mart is well-positioned to navigate the uncertainty. Unlike much of the industry, America's Car-Mart conservatively underwrites its own loans, maintains strong relationships with customers, and has effective recovery processes available, if needed. We believe that because auto transportation is a necessary means to get to work, consumers will make a great effort to meet minimum car payments. Further, because Car-Mart tries to direct its buyers to vehicles they can afford, this economic shock will not just reduce absolute risk, it may well lead consumers to make more fiscally responsible purchases in the future. That would drive more volume and long-term relationships to Car-Mart's dealerships. Finally, the US consumer should benefit from direct government payments in the interim. We increased our position in the company during the quarter.

Solaris (SOI) adds tremendous value to its oil and gas customers through innovative solutions, but they were not immune to the pressures facing the industry. While near-term fundamental declines driven by commodity prices is inescapable, a strong balance sheet, defensible business model and a high returns-focused management team make Solaris a tremendous long-term opportunity.

CNX Midstream (CNXM) has a very stable pipeline business model governed by long-term fixed-fee agreements on gas recovered by its customers. The extreme stress in the commodity pricing environment, along with anticipated volume declines, negatively impacted the stock price. One unrelated development during the quarter, though not a significant driver to the price decline, was that they announced a new incentive distribution rights (IDR) agreement with their GP, CNX Resources. While this agreement involved issuing equity at a premium, the overhang on the stock is a clear positive going forward.

CIT Group (CIT), like other banks, is economically sensitive, but it was walloped due to its exposure to small-medium business, aircraft financing and rail leasing. We expect that the government backstop has mitigated some of the most-feared risks. We believe the long-term opportunity remains intact, as they gradually transform into a more traditional bank. At current valuation (0.31x book), the stock is undervalued by any measure, most especially if they can reach 13%-14% returns on equity targeted by management in the next few years.

Northern Technologies (NTIC) is a consumable products company used widely by European auto manufacturers. With auto production stalling during the shutdown, the company will experience a significant slowdown. While the near-term pressure on sales is inescapable, the long-term outlook for business and market share remain differentiated and intact. Further, they continue to have very attractive

growth opportunities in their aboveground storage tank bottom protection and Natur-Tec compostable plastics divisions. This is an asset-light business with no debt and $2.40 per share in cash on the balance sheet, accounting for one-third of the company's value at quarter-end.

Concluding

Thanks again for your interest in Ballast. If you have any questions about our firm, our team, or our strategy, please reach out to us. www.ballastam.com

Until next time, stay positive, stay healthy, and remember we are in this together. Recessions each have their unique set of circumstances, but they all end in a recovery.

Regards,

Ragen Stienke

Important Notes and Disclosures

The investment decisions we make for clients' accounts are subject to various market, economic, and other risks, and there is no guarantee that those investment decisions will always be profitable. Clients are reminded that investing in any security entails risk of loss, which they should be willing to bear. The past performance of the firm or its principal is no guarantee of future results.

Some information contained in this communication was obtained from third-party sources. While these sources are believed to be accurate, that information has not been independently verified.

[1] The Ballast Portfolio represents the performance of a composite of accounts invested in the firm's model strategy that was launched on August 11, 2015. Gross Performance represents the returns of the composite after all expenses, but before deduction of management fees. An individual client's account would be subject to the deduction of management fees in accordance with the Ballast fee schedule. Net Performance represents returns net of all expenses and the highest management fee rate (1%) in the firm's fee schedule. The returns achieved by an individual client's account may vary from those reported for various reasons, including management fee rate, timing of cash flows, frequency of rebalancing of individual accounts, and an individual client's restrictions. In April 2019, Ballast transitioned from calculating performance based on a proprietary account to composite. The composite performance should be the sole source of information used when evaluating past performance. Past performance does not guarantee future results.

[2]The Russell 2500 Value Index measures the performance of those Russell 2500 companies with lower price-to-book ratios and lower forecasted growth values. Returns shown include the reinvestment of dividends and are based on data obtained from FTSE Russell.

[3]The Russell 2500 Index is a market capitalization weighted index of the 2,500 smallest companies in the Russell 3000 universe of United States equities. Returns shown include the reinvestment of dividends and are based on data obtained from FTSE Russell.