STERN IAG

Board of Advisors Meeting

Oct 4th, 2021

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Letter from Portfolio Managers

Dear Board of Advisors,

We are very excited to be kicking off the new IAG year, especially now that we are nearly fully back in-person! Over the past four weeks we have worked to fully implement and incorporate several of our investment process improvements from last year, including the role of a "devils advocate" on ideas approaching oversight.

Since our last meeting in April 2021, the market has mostly continued it's post-COVID rebound through the summer, with only September seeing a sell-off across the broader market indices. While the S&P 500 return over this summer has been ~+3.02%, there is still a lot of uncertainty regarding the trajectory in the market. Investors have been acutely focused over the past several weeks on the recent distress of Chinese real estate company – Evergrande Group – as well as concerns here in the US with the federal government's debt ceiling standoff. Underlying all these other concerns are the ongoing issues of rising inflation rates and commodity input prices.

Bearing these macro risks in mind, we will be both watching our legacy positions more closely while also looking for new ideas in more defensive industries over the upcoming semesters. As a result, we are today asking to exit two of our legacy positions which have substantially underperformed our benchmark (Grocery Outlet and Recro Pharma) and are hoping to replace them with more defensive new ideas (Builders FirstSource and Flex Ltd.).

Overall, we are happy with IAG's recent performance, which as returned +53.14% on an LTM basis, beating the S&P 500 benchmark return of +36.30% by 16.84%, although we attribute most of this outperformance to our heavy small to mid cap and industrial bias.

We would also like to take a moment to thank Prof Brad Hintz for his very generous $10,000 donation to the Fund, which has brought our AUM to ~$83,300. We are incredibly grateful for his confidence in our process, as well as providing us the unique challenge of deciding how to best allocate fresh capital in a portfolio. We have taken much time discussing this question internally these past several weeks and have ultimately decided that rather than double down on several of our previous positions – which we may well still do should an opportunity arise – we would instead like to pursue fresh and new ideas to avoid thesis creep and keep our portfolio up to date.

Today, we are pleased to present the following businesses that exemplify our investment philosophy:

1. Builders FirstSource (NYSE: BLDR) — a leader in the scaled building materials rolling up pre-fabrication assets
2. Flex LTD. (NASDAQ: FLEX) — an electronics manufacturing services (EMS) company with a promising solar asset

We look forward to the remainder of the semester and are more than happy to continue being a source of information to the Board and encourage you all to reach out with feedback or clarifications at any time.

Best,

Caleb Nuttle & Tony Wang

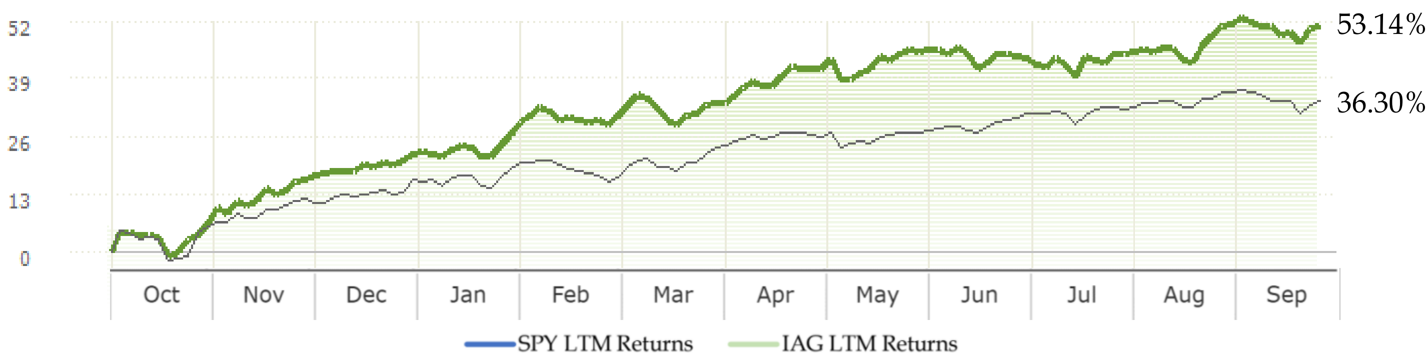
Portfolio Managers

II. Performance Analysis

Holdings Summary *(as of Sept 27th, 2021)*

Current Holdings											
Company Name	Ticker	Coverage	Date of Purchase	% of Portfolio	Share Count	Price At Purchase	Share Price	Current Return	Morningstar Industry	Holding Type
Allison Transmissions	ALSN	Cody Fang	12/3/19	**2.2%**	50	$47.72	$36.13	(24.3%)	Consumer Cyclical	Core
APi Group Corp	APG	Srikar Alluri	9/24/20	**4.0%**	160	$14.29	$21.03	47.2%	Industrials	Core
Berry Global Group Inc	BERY	Sophie Pan	12/2/20	**3.8%**	50	$54.60	$62.45	14.4%	Consumer Cyclical	Core
Concrete Pumping Holdings Inc	BBCP	Cody Fang	3/26/21	**3.2%**	300	$7.07	$8.84	25.0%	Industrials	Core
CVS Health Corp	CVS	Srikar Alluri	12/16/16	**2.1%**	20	$77.28	$85.74	11.0%	Healthcare	Core
Exelon Corp	EXC	Rhys Berezny	4/30/21	**4.1%**	70	$44.83	$48.89	9.1%	Utilities	Oppt.
FirstEnergy Corp	FE	Simran Korpal	10/29/19	**2.2%**	50	$45.66	$36.72	(19.6%)	Utilities	Core
Grocery Outlet	GO	Amy Chen	5/14/20	**1.3%**	50	$36.75	$22.05	(40.0%)	Consumer Defensive	Core
GXO Logistics Inc	GXO	Tony Wang	8/2/21	**4.2%**	45	$32.21	$78.55	143.9%	Industrials	Core
HCA Healthcare Inc	HCA	Srikar Alluri	9/26/19	**5.8%**	19	$119.99	$255.55	113.0%	Healthcare	Core
Identiv Inc	INVE	Tony Wang	9/24/20	**9.7%**	400	$5.68	$20.16	254.9%	TMT	Oppt.
JD.com Inc ADR	JD	David Zhou	4/30/21	**3.7%**	40	$77.55	$76.43	(1.4%)	Consumer Cyclical	Core
Methode Electronics Inc	MEI	Achyut Seth	2/19/21	**4.2%**	80	$38.56	$43.27	12.2%	TMT	Core
Office Properties Income Trust	OPI	Cody Fang	10/28/20	**4.1%**	130	$17.85	$26.05	46.0%	Real Estate	Oppt.
Palo Alto Networks Inc	PANW	David Zhou	9/24/20	**5.8%**	10	$240.50	$486.04	102.1%	TMT	Core
Points International Ltd	PCOM	Tony Wang	10/28/20	**5.0%**	240	$10.01	$17.16	71.4%	TMT	Oppt.
Recro Pharma Inc	REPH	Srikar Alluri	10/29/19	**0.4%**	160	$7.30	$2.07	(71.7%)	Healthcare	Oppt.
TransDigm Group Inc	TDG	Jaro van Diepen	4/9/20	**2.3%**	3	$362.96	$648.82	78.8%	Industrials	Core
United Rentals Inc	URI	Caleb Nuttle	3/14/19	**6.2%**	14	$114.85	$365.84	218.5%	Industrials	Core
XPO Logistics Inc	XPO	Tony Wang	10/20/19	**4.6%**	45	$42.87	$85.31	99.0%	Industrials	Core
ZTO Express	ZTO	David Zhou	3/14/19	**3.8%**	100	$19.43	$31.67	63.0%	Industrials	Core
Total Equity Holdings				**82.6%**			**$68,765.07**			
Cash				**17.4%**			**$14,517.65**			
Total Portfolio Holdings				**100.0%**			**$83,282.72**			

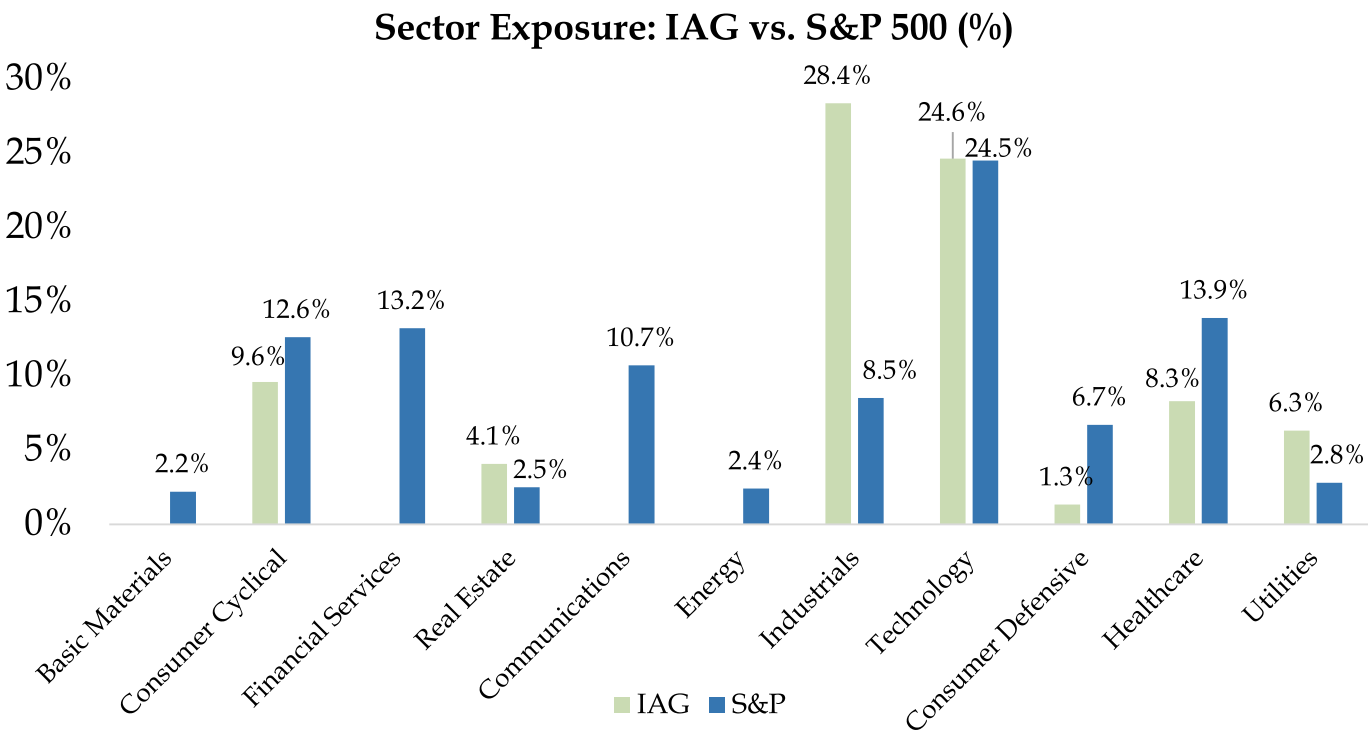
IAG vs S&P 500 LTM Returns

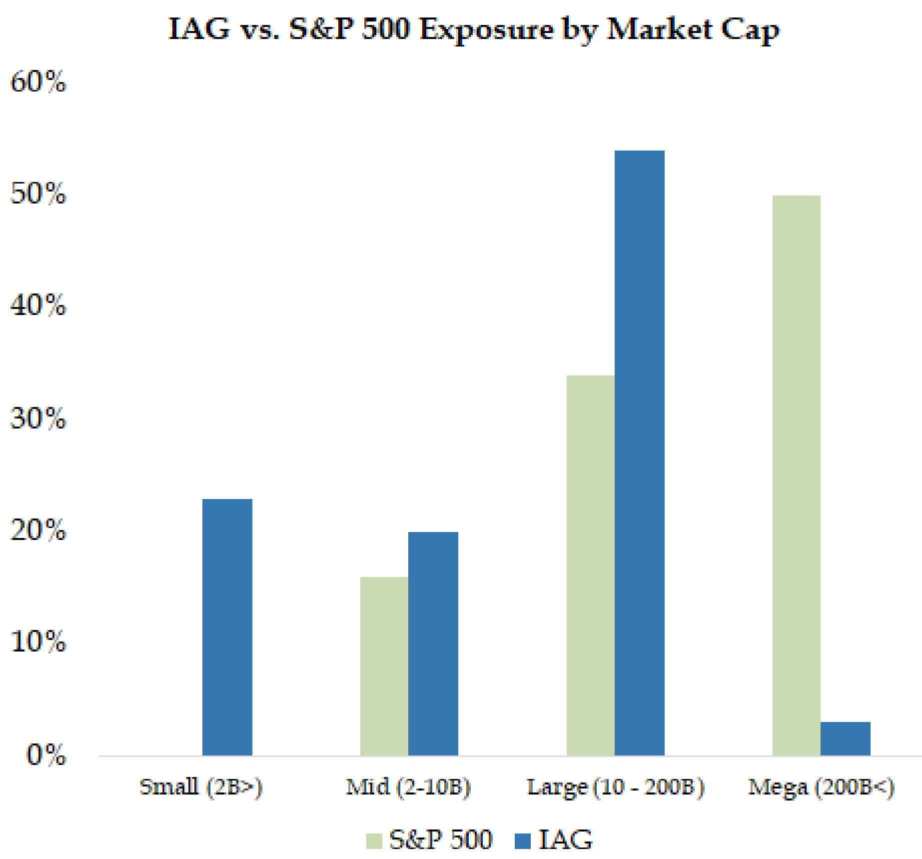


On a last twelve-month basis, **IAG's portfolio has returned 53.14%** while the S&P 500 returned 36.30%. Since the last oversight meeting, **the spread between IAG's portfolio and the S&P 500 contracted from 21.03% (4/30/21) to 16.84% (10/4/21).**

Our opportunistic positions now represent ~23% of our portfolio which is in line with our expectations.

Portfolio Exposure vs. Benchmark





IAG continues to use the S&P 500 as the core benchmark as specified in the fund mandate. While our industrial exposure is still substantially overweight, the two proposed positions today will help improve the composition.

IAG continues to be underexposed to mega-cap positions, yet drastically overexposed to small-cap companies. We will continue to look at the mega cap space for potential opportunities but do not think that the underexposure poses a major issue.

Pitch Log Since Apr 2021 Meeting

Internal Pitches Since Mar 2021 Meeting

	Company	Stage	Date	Analysts
1	**CoStar Group Inc.**	**Quick Screen**	**9/9/21**	Niranjan Narasimhan
2	**Monster Beverage Co.**	**Quick Screen**	**9/9/21**	Achyut Seth
3	**Flex Ltd.**	**Quick Screen**	**9/9/21**	Rhys Berezny
4	**Builders Firstsource**	**Quick Screen**	**9/9/21**	Rahul Parikh
5	**Grocery Outlet**	**Position Update**	**9/16/21**	Amy Chen
6	**Peloton Interactive, Inc.**	**Quick Screen**	**9/16/21**	Alice Yu
7	**AT&T Inc.**	**Quick Screen**	**9/16/21**	Alex Isaac
8	**Keurig Dr. Pepper**	**Quick Screen**	**9/16/21**	Caleb Nuttle
9	**Grocery Outlet**	**Position Update**	**9/23/21**	Amy Chen
10	**Builders Firstsource**	**First Update**	**9/23/21**	Rahul Parikh
11	**CoStar Group Inc.**	**First Update**	**9/23/21**	Niranjan Narasimhan
12	**Flex Ltd.**	**First Update**	**9/23/21**	Rhys Berezny
13	**CDK Global Inc.**	**Quick Screen**	**9/23/21**	Jaro van Diepen
14	**Flex Ltd.**	**Second Update**	**9/30/21**	Rhys Berezny
15	**Flex Ltd.**	**Devil's Advocate**	**9/30/21**	Tony Wang
16	**Builders Firstsource**	**Second Update**	**9/30/21**	Rahul Parikh
17	**Builders Firstsource**	**Devil's Advocate**	**9/30/21**	Caleb Nuttle, Mikhail Talib

Active Pipeline and Bench

	Company	Stage	Date	Analysts
1	**Monster Beverage Co.**	**Quick Screen**	**9/9/21**	Achyut Seth
2	**Peloton Interactive, Inc.**	**Quick Screen**	**9/16/21**	Alice Yu
3	**AT&T Inc.**	**Quick Screen**	**9/16/21**	Alex Isaac
4	**Keurig Dr. Pepper**	**Quick Screen**	**9/16/21**	Caleb Nuttle
5	**CoStar Group Inc.**	**Quick Screen**	**9/23/21**	Niranjan Narasimhan
6	**CDK Global Inc.**	**Quick Screen**	**9/23/21**	Jaro van Diepen

Oversight Meeting

	Company	Stage	Date	Analysts
1	**Flex Ltd.**	**Second Update**	**9/30/21**	Rhys Berezny
2	**Builders Firstsource**	**Second Update**	**9/30/21**	Rahul Parikh

III. Key Holdings Update

Portfolio Updates Since Apr 2021 Meeting

Company	Ticker	Update
Allison Transmissions	**ALSN**	We propose holding our position in Allison Transmissions. The original thesis is still intact as the business is slowly gaining market share in the class 4 and 5 markets and has been increasing its next generation transmission offerings for electric vehicles. Management has previously hinted at revealing formalized EV collaborations with major OEMs in the back half of 2021. Further, the company remains confident that there are a limited number of parties that can provide a full suite of propulsion solutions in the medium and heavy-duty market. Solid performance in Q2 2021 in the North America on-highway market (+84.1%) demonstrated strong end market demand despite supply chain shortages. The general expectation is for supply chain shortages to ease in 2022 with the company passing on 110bps of price in 1H 2021 and a further increase of ~200bps in price in 2H 2021. Overall, we remain confident that Alison can continue to dominate the market while providing EV propulsion solutions.
APi Group	**APG**	The APi group recently acquired Chubb, a non-core division of Carrier specializing in fire safety services. We had anticipated the company making larger acquisitions as part of our thesis and have seen the results as the fire safety mix will grow from 40% to 65% when the acquisition closes later in the year. APi business trades at 12x EV/EBITDA. We still see multiple expansion from the current levels as smaller fire safety inspection platforms trade at between 15-20x. We also are opportunistic on the company's ability to improve the margins of Chubb from 9% to 12% or more.
Berry Global	**BERY**	We propose a hold in our stake in Berry Global. The original thesis was based on deleveraging through free cash flow and continued organic growth in their four segments. In terms of leverage, the company has achieved their goal of sub-4x leverage before the end of FY21. From 4.3x at the beginning of FY21 to 3.9x net debt to adj. EBITDA most recently reported, we believe investor concerns over high levels of debt associated with the $6.5bn acquisition of RPC in 2019 are no longer material. The company will maintain leverage at 3.0-3.9x and consistently rakes in 8% FCF yield. Berry also saw 5% organic growth, attributable to the recovery of their Engineered Materials segment (industrial market, saw segment organic growth of 8%) which previously faced COVID-19 headwinds. The company also continues to position itself at the forefront of sustainability, framing it as a growth opportunity, which will alleviate the market misconception about plastics. We expect plastic packaging to comprise 40+% of the global packaging market by 2025. As a large plastics producer with scale, opportunities still exist in faster growth markets, emerging markets, sustainability, and flexible plastics. In terms of supply chain cost increases and inflation, Berry saw a decrease in operating income due to unfavorable price cost spreads. The company experienced inflation in raw materials and freight, but passed costs throughcontracts. The unprecedented resin inflation was offset by volume growth and incremental cost for product delivery. Berry expects a modest incremental inflationary impact over the next few quarters, and this effect is not unique to the firm nor will it materially affect the long-term organic growth.
Brundage-Bone Concrete Pumping Holdings	**BBCP**	We propose holding our stake in Brundage-Bone Concrete Pumping. Our position is up 24.9% since our purchase at $7.08 per share. BBCP has continued to perform as the tier 1 operator in the concrete pumping industry. The company generated healthy revenue growth of 5% year-over-year in the third quarter, driven by demand in residential and infrastructure markets. Eco-pan revenues grew 8% from organic growth and pricing improvements. In the UK, recovery tailwinds fueled revenue growth to 37%. BBCP has also successfully continued its M&A strategy, acquiring Houston-based pumping company Hi-Tech. In Southern California, the company purchased an additional 16 booms from HDCE. BBCP still has a ~$100 million EBITDA acquisition pipeline which they will deploy over the next few years targeting 4x EBITDA transactions. By optimizing supply chain discounts and other OpEx synergies, BBCP will continue their success in increasing margins. The greenfield expansion into the Las Vegas market is a primary focus for management, providing opportunities for revenue growth in the coming years. A team has been put together, with excess equipment being redirected to the area. While BBCP faced weather disruptions in key markets such as Texas and Colorado, organic growth in other regions offset losses. In all, BBCP's performance in the last quarter has strengthened our thesis and provided results justifying a continued position.

Portfolio Updates Since Apr 2021 Meeting

Company	Ticker	Update
CVS Health	**CVS**	We propose a hold in our stake in CVS. Our original thesis centered around CVS' competitive positioning in the oligopolistic PBM market and ability to maintain margins. In the most recent quarter, total revenues of $72.6 billion grew 11% YoY, reporting adjusted operating income of $4.9 billion and adjusted earnings per share of $2.42. Health care benefits revenue increased 11% YoY driven by CVS' continued growth in the government services business, slightly offset by the repeal of the health insurance fee or HIF. CVS' pharmacy services delivered 9.8% revenue growth, maintaining 98% retention rate with ≥ 80% renewals completed. The prescription market share grew to over 26%, while store sales saw a strong rebound momentum, increasing nearly 13% in the quarter, primarily driven by network volume and specialty pharmacy growth. Tailwinds for CVS include strong selling seasons in the pharmacy services segment and in commercial national accounts in the healthcare benefits segment. Headwinds include consistent pressure in Pharmacy Services from client price improvements and reimbursement pressure in retail; the impact of annualizing the increase to minimum wage across the company; and uncertainty regarding the expected revenue from COVID vaccines and testing in retail operations.
Exelon Corp	**EXC**	We propose holding our position in Exelon. The original thesis is still intact and, most importantly, we are waiting for February 2022 when the spin-off takes place. There have been no material changes to current overall operations. The regulated utilities side has been performing strong as usual and continues to outperform other comps both operationally and financially. For generation, there were some very poor results in Q1 given the power outage in Texas which caused a 90 cent per share loss just due that event alone. Q2 was much better for both businesses as both outperformed expectations. One quite worrying element in the Q2 earnings call was the early retirement of the Dresden and Byron plants as there was no progress or regulation passed towards keeping them open; they were set to close in just a few weeks. Luckily, given the plants' major influence on the Illinois job market and power generation market in Illinois, they were saved by a clean energy omnibus package that includes $694 million in assistance to these plants over the next five years.
First Energy	**FE**	We would like to propose to hold FE given the recent shift in corruption investigation news. First Energy has come to an agreement with the US Attorney's Office for the Southern District of Ohio to resolve the Department of Justice's investigation into FirstEnergy. The agreement is a deferred prosecution agreement where First Energy pays $230 million and provides regular updates to the government on internal controls and compliance. In relation to this the company hired a new Legal Officer and Compliance Officer. Additionally, Icahn Capital entered the business in March and they are awaiting voting rights pending regulatory approval. Turning to the company's operations, First Energy announced Q2 2021 Earnings and came in on the high end of their operating earnings. Additionally, as the company moves forward they will begin to execute the third phase of FE forward which should unlock value with free cash flow improvements of roughly $800 million in 2021 through 2023.
Grocery Outlet	**GO**	**Sell note in packet**

Portfolio Updates Since Apr 2021 Meeting

Company	Ticker	Update
GXO Logistics	**GXO**	We propose a hold in our stake in GXO, up ~45% since inception. We entered this position as a result of XPO's spinoff during the summer. The spin separated the LTL business from the logistics contracting business. While much of the original SOTP discount we originally identified has closed, we still believe that GXO is a premium asset with sustainably higher ROIC than competitors. Further, there are strong secular growth drivers in North American and European logistics markets that GXO should continue to enjoy. As incremental ideas are added to the portfolio, we will look to phase GXO out. However, we believe that it is relatively more attractive than cash at today's levels and propose a hold.
HCA Healthcare	**HCA**	We would like to propose a hold on HCA, the business has been able to recover from the depths of the pandemic and has resumed its capital deployment through acquisitions and resumption of its share buyback and dividend. We have also seen the company acquire the home health business of Brookdale Senior Living which we see as the further development of HCA expanding into higher-growth areas. The multiple on the business has expanded to 9.5x, but we still see further expansion as we think the company is a better operator than its peers. In the short term, we are monitoring a slowdown in elective procedures due to the Delta variant and the rising nursing costs, but we are confident that these issues are temporary.
Identiv	**INVE**	We propose a hold in our stake in INVE, up ~200% since inception. The business is effectively capitalizing on RFID market trends, as promised by management last year. The ability to ramp up incremental capex makes the future growth highly margin accretive. It is evident that the business has signed several behemoth customers (Apple, CVS, etc.), all of whom are moving new product iterations or supply chain initiatives to the RFID NFC space. The TAM is still nascent and Identiv's early start and established relationships are key competitive advantages going forward. Smartrac, the closest NFC comp, lost its head BD executive to Identiv, another positive development. Another notable update since our prior meeting is that Identiv has been selected for Russell 2000 inclusion and the buying pressure and institutional attention has contributed to the upside here.
JD.com	**JD**	We propose to hold our position in JD. The company's fundamentals remain strong despite regulatory concerns. In the second quarter, JD achieved GMV growth of 27.7% yoy, sustaining the recovery momentum of the retail market in China. In terms of user base, annual active usage increased by nearly 32M with improvement in retention rate, shopping frequency, etc. LTV total active users reached 532M, up 27% YoY. Penetration of the lower-tier cities is well under way, with 80% of new users coming from this group. The Jingxi new business segment in particular saw triple digit growth over the quarter, and in management's the business on track to serve price-sensitive customers. We are confident concerns over China regulation will gradually dissipate as the Chinese government has never meant to crack down or restrict Internet firms but to rationalize the industry, and price would again follow business fundamentals.

Portfolio Updates Since Apr 2021 Meeting

Company	Ticker	Update
Methode Electronics Inc.	**MEI**	We propose to hold our position in Methode Electronics, which is up 12.2% since our investment in February, because there are no significant changes in our investment thesis despite ongoing headwinds with supply chain issues, such as the semiconductor chip shortage and port congestion. Although these headwinds put downward pressure on sales and margins, organic growth was up 45% YoY in the latest earnings (Q1 2022) and management returned value to shareholders by raising the dividend and repurchasing $7.6 million of shares in the quarter. Additionally, our thesis of top-line growth through an increasing allocation of capital towards EV continues to be supported, as sales into hybrid and EV applications were 16% of total sales. Furthermore, Methode continues to diversify from its customer consolidation with GM and Ford, as the company's operations outside of these two clients grew to ~64% of annual sales in 2021. Although management forecasts performance to be below the midpoint of ranges provided by guidance, we believe Methode Electronics's value proposition as a specialized one-stop shop with competitive margins is strong enough to withstand the short-term headwinds.
Office Property Income	**OPI**	We propose holding our position Office Properties Income Trust (OPI). Since our entry point, OPI's portfolio of attractive properties with high credit-grade tenants has significantly improved with the acquisition of a class A Google office in Chicago (531,000 rentable square feet, $355 million at a cap rate of 4.7%, 6.6 year WALT) and a class A office building Atlanta which is the headquarters for Insight Global. (346,000 rentable square feet, $195.0 million at a cap rate of 6.3%, 14.2 WALT). These two acquisitions show that the business and management is capable of effectively executing the capital recycling strategy. The attractive dividend remains intact and has been paid out in full each quarter since we made the purchase. No significant updates to be made in this regard.
Palo Alto Networks	**PANW**	We propose a hold on Palo Alto Networks. The company had their FY21 Q4 earnings call on August 23rd, where they announced that revenues had increased by 25% YoY and forecasted similar growth for FY22. The growth was largely driven by an 81% YoY increase in Next-Generation Solutions (Prisma and Cortex products) ARR and a 47% increase in the number of Prisma Cloud customers, validating our thesis that Palo Alto Netowrk's move into cloud-based security products would provide for significant growth. Based on these results, the company's stock price jumped by 18% on August 23rd, resulting in a total gain of 35.5% since the last oversight meeting. On the M&A front, CEO Nikesh Arora stated that PANW would likely not continue the aggressive acquisition pace that it had set in the last couple of years. The company has validated our thesis that it would become a dominant one-stop cybersecurity shop with offerings across multiple industry verticals. As a result, there isn't a current need to grow into new spaces as there was in years past. We propose to hold as the company's fundamentals are strengthening and there's still much growth ahead for the new businesses.
Points International	**PCOM**	We propose a hold on PCOM. Airline volumes are the key KPI to watch for this business, albeit slightly backward looking (loyalty points already expensed). We are encouraged by rapid recovery in TSA checkpoint volumes. Further, the business has been able to successfully sign several large partners since our position's inception. There is ample runway within each of these new partner relationships and the existing base to cross-sell functionality, with the most saturated customers still only leveraging a fraction of PCOM's total product suite. PCOM is still trading at a LDD normalized FCF multiple, using 2019 levels as a proxy. We believe the runway is still quite promising for the business and can underwrite a mid-teen's IRR from these levels.

Portfolio Updates Since Apr 2021 Meeting

Company	Ticker	Update
Recro Pharma	**REPH**	**Sell note in packet**
TransDigm Group	**TDG**	We propose we hold our position in TransDigm. With passenger volumes having recovered to ~80% of 2019 volumes, TDG's OEM, aftermarket and defense segments are approaching 2019 levels. In the commercial OEM business, management expects demand to be reduced in the short term but positive commentary from the OEMs around narrowbody production is promising. Additionally, capital deployment will be a key area of focus as TDG has called off its plan of acquiring Meggitt, which would have been its largest acquisition (2.5x Esterline). Even if management cannot find another attractive M&A target, however, there are other avenues of attractive capital allocation such as addressing the higher that historical average debt load (net debt/EBITDA of 8.5x) that was assumed as a safety measure when COVID started.
United Rentals	**URI**	We would like to propose holding our stake in United Rentals (URI) at $359.98, up 213.43% since inception in March 2019. While the position has certainly performed well within its industry, we still believe the company trades at an unfair discount to other construction equipment companies, such as CAT. United Rentals currently trades at 13.9x EV/EBITDA. This is overall at a discount to Caterpillar, which trades at 14.8x EV/EBITDA. This is despite the fact that the equipment rental business model is more attractive in the US' current construction economic environment, where economic activity has slowed and construction project volume is down, making it harder to justify a purchase of new construction equipment rather than simply rent. Additionally, URI's management has continued their promise to focus on decreasing leverage rather than revert to their historic acquisition heavy strategy. Overall, while the market has certainly realized a portion of its previous discount, we still believe URI is a position worth holding. We believe that it should be considered as one of the portfolio's core holdings, especially within the industrial holdings.
XPO Logistics	**XPO**	We propose a hold on XPO logistics and a hold/sell on its spin off, GXO logistics. On August 2nd, XPO successfully completed the spin off of its pure-play logistics contracting business and shareholders received one share of the new company, GXO Logistics, for every share of XPO they owned. Since the spin off, XPO shares are down 5.2% and GXO shares are up 43.9%. The spin off allowed XPO to increase its exposure to the attractive less-than-truckload (LTL) space, which we mentioned in our initial thesis as being undervalued by the market. North American LTL now accounts for 35% of XPO's revenues. Still trading at a discount relative to other non-unionized LTL companies such as Old Dominion Freight Line and Saia, we believe there is still upside in holding XPO.
ZTO Express	**ZTO**	We propose to hold our stake in ZTO. The company delivered solid performance in 2Q 2021. Parcel volume grew by 25.6% while revenue grew by 14.4% to RMB 7.3 million. This gap in volume and revenue growth is due both to ASP decline as a result of competition (-5.9% drop in ASP) and weight per parcel decline (-8%). Unsurprisingly, margins eroded as price headwinds more than offset cost efficiencies. However, ZTO continues to outperform the other Tongda peers and has expanded market share from 20.4% at the end of 2020 to 21% by the second quarter. The firm is continuing its capital investments in delivery infrastructure to facilitate future growth. The price war and margin headwind come within our expectations and our view on the firm has not changed. With its scale and prudent investments in automated sorting hubs and trucks, ZTO is on track to become the future monopoly in the industry as the cost leader.

IV. Sell Notes

Sell Note: Grocery Outlet (NYSE: GO)

Dear Board of Advisors,

We would like to sell **out** of our current position in **Grocery Outlet (NYSE: GO)**, representing **40% downside**. We initially invested in the company for its thesis points of 1) leadership in discount grocery, 2) uniquely flexible sourcing/distribution model, 3) localized business with reduced operational risks, and 4) consistent store growth. Recently, the business has reacted quite negatively to the combination of COVID recovery and consolidated grocery trips and increased basket sizes. Grocery Outlet's share price fell over the summer following the Q1 and Q2 earnings releases, and we believe it is time to cut our losses.

We believe that our original thesis points can no longer stand against recent headwinds. These factors likely led to Grocery Outlet's disappointing comparable store sales, especially compared to other grocers (Fig 2). Overall, the company no longer appears to be providing an attractive growth opportunity for the near future.

Consolidating Grocery Trips: Management initially expected the dynamic between lower traffic and higher tickets from COVID to invert with recovery. Instead, what they saw in the first two quarters of 2021 was the decrease of both traffic and ticket size while other grocers retained both customers and higher basket sizes. We are pessimistic about this trend of consumers favoring larger basket sizes, especially spurred by growth in grocery ecommerce, reversing in the near future. (Management has mentioned ecommerce in GO's future but have expressed concerns about translating the store's value proposition online at cheap prices.) Since Grocery Outlet focuses on bargain groceries with rapid expiration dates, consolidated basket sizes are anathema to their business model, diminishing their competitive advantage against traditional grocers.

Additionally, we see short term erosion in GO's value proposition as larger grocers step up promotional activity. Combined with robust stimulus from the federal government, the company's value proposition is no longer a competitive advantage.

Margin Compression: Macroeconomic trends such as inflated labor, freight, and commodity costs have recently brought rising costs. Additionally, IO turnover has also increased this year over a year ago. Management cited labor shortages and safety concerns over the Delta variant leading to stressed IOs. These factors have likely contributed to Grocery Outlet's lower recent productivity in 21Q2 (~62% productivity rate) compared to historical rates (2019: ~68%, 2020: ~83%, 21Q1: ~73%). Thus, the market has priced in these factors relating to margin compression

Since our purchase in Grocery Outlet, many of the thesis points continue to successfully play out. The company's fundamentals have not changed, and it continues to expand with 10% new stores annually. However, the largest concern of consolidating basket sizes does not appear transitory with consumers getting used to the ease of shopping online and retaining pandemic habits. Thus, we feel it is best to exit the position at this time and cut our losses for the portfolio.

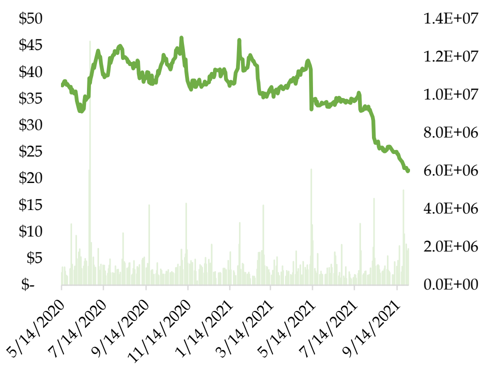
Best,

Amy Chen

Stock Overview (LTM Figures)

	At Purchase:	Current:
Share Price	36.75	22.05
Sales ($mm)	2,714	3,099
EBITDA %	6.4%	5.5%
ND/EBITDA	5.6x	4.6x
EV/EBITDA	36.5x	21.3x

Performance Since Purchase on X



Same Store Sales for Grocery Retailers

		3 Month Period	2 Year Period
21Q2	GO	-10.0%	6.7%
	ACI	-10.0%	16.5%
	NGVC	-3.6%	11.9%
	WMT	5.2%	14.0%
	TGT	8.9%	36.0%
	KR	-0.6%	14.0%
20Q2	GO	16.7%	22.4%
	ACI	26.5%	28.0%
	NGVC	15.5%	17.9%
	WMT	9.3%	13.8%
	TGT	24.3%	27.7%
	KR	14.6%	16.8%
19Q2	GO	5.7%	-
	ACI	1.5%	1.7%
	NGVC	2.4%	7.6%
	WMT	4.5%	9.0%
	TGT	3.4%	10.0%
	KR	2.2%	3.8%

Sell Note: Recro Pharma (NASDAQ: REPH)

Dear Board of Advisors,

We would like to **sell our entire position of Recro Pharma (REPH)**. While an argument could be made that this opportunity has an asymmetric upside/downside case, we believe that ultimately, the business fundamentals have diminished enough over COVID that this no longer represents an attractive opportunity.

In early 2019, peer CDMO Brammer Bio was purchased for $1.7bn in cash while the company generated $250mm in revenues. Later that year, another CDMO CBM was acquired for 16x EBITDA for $2.5bn. **Recro, trading significantly under both of these companies, became a popular pick amongst value investors and hedge funds for the reason that the stock price was severely dislocated.** This was the most significant part of our thesis, given the company traded at just 6-8x EBITDA while comparable M&A was degrees higher. CDMOs were attractive for having high switching costs and supported by tailwinds that pushed pharma companies to outsource R&D. However, as COVID mounted, it was clear that many of these competitive advantages deteriorated and the company was not as insulated as many investors thought. With mounting debt, the company's share price fell quickly as it posted close to 0 EBITDA margins throughout 2020. Originally, we argued that the business was an attractive PE target because of predictable and constant cash flows. Throughout COVID, this thesis point was disproven as costs ran wildly high and we no longer believe that this company is an attractive target for acquisition, and even if it was, the acquisition would not be significantly accretive to the value of the company.

The next part of our original thesis was the attractiveness of the CDMO business. Throughout COVID, the business was heavily squeezed by its partner pharma companies. Given the company also has a large portion of costs fixed, the inability to adjust to the decrease in demand led the company into a precarious position as it was also highly levered. Being in the small molecule space with limited biologics exposure, we found the company to have a much tougher position than originally anticipated.

We also have several non-thesis related reasons for our sell note.

Management is misaligned. Management owns very little/no stock and has not been purchasing on the open market since the stock dipped. Additionally, the board continues to vest shares to the CFO without any indication that the company has hit performance targets. Furthermore, Arnaud Ajdler, the chairman of Engine Capital, an activist hedge fund, owned about 1 million shares. However, he resigned as a director of Recro and has since sold almost almost all of his shares in the business. This further confirms the inability for REPH to realize an M&A case.

It is also especially important to note that new management is uninspiring, and we do not have a "free option" as we thought we once had in their ability to write a new contract. Throughout the summer, where we thought most of the downside was baked into REPH, it ended up falling more than 30%, making this option costly, especially since we have lost faith in management's ability to find a new contract to underwrite.

Overall, being equity holders in this business is not attractive. Recro Pharma has also recently issued over 2 million shares via recent S-3, creating a $100mm shelf that we believe is not accretive to our position as equity holders when the underlying fundamentals in the first place are not supremely attractive. In addition to the S-3 shelf, the company has also been trading debt off its balance sheet for equity. Arythium was issued $9mm equity in exchange for the business to de-lever by $25mm. These equity issues are nothing new, and impacts are very real - in 2019, REPH had some 23mm shares outstanding, diluted now to 47mm shares. Considering all these factors, we would like to sell this position.

Best,

Vinny

Stock Overview (Forward)

	At Purchase:	Current:
Share Price	$13.20	$2.05
Market Cap	307.5	95.6
EV	398.5	116.7
Net Leverage Ratio	2.7x	17.5x
EV/EBITDA	6.2x	8.4x

Performance Since Purchase on 10/29/19

V. New Position Proposal

Builders FirstSource, Inc. (NYSE: BLDR)

Dominant industry position with strong track record, attractive growth prospects

Rahul Parikh
Junior Analyst
rkp7593@nyu.edu

Price Target: $77.57 (43.3 % Upside)

September 29th, 2021

Business Description:

Builders FirstSource is a distributor and manufacturer of lumber, building material products, and other building supplies across the United States. They operate in 500+ locations across the country, including 85 of the top 100 MSA's. Balanced end-market exposure (72% sales to new SF Housing / 22% R&R / 6% MF housing). The top 10 customers accounted for approximately 15.8% of net sales, and no single customer accounted for more than 6% of net sales.

Investment Thesis:

- **BMC merger significantly upgrades scale, adaptability, and leverage:** BLDR completed its 'super merger' with BMC Construction earlier this year. The merger makes BLDR the largest player in the US space and fleshes out their product line to meet all homebuilders needs. Specifically, BMC fills out the holes in the manufactured products that BLDR offers and adds leverage to the notoriously volatile lumber supply chain. Both segments show significant growth in Q1 2021 (post-acquisition). This makes BLDR the only supplier of its scale with a full product line and adds to their geographical footprint. BLDR is now fully integrated down the value chain, solidifying itself as a one stop shop for homebuilders marks an industry shift. Historically, homebuilding companies and independent builders would use multiple services for different products (e.g., Roofing, Lumber, Turn-Key Services). With the industry trending towards consolidated suppliers, BLDR is now the obvious choice. BLDR's track record with acquisitions is very strong. Previous acquisitions have proved to be accretive and quickly integrated, comparatively to peers. In 2014/2015, BLDR completed their major ProBuild acquisition, along with 7 small scale acquisitions. After the initial year of high overhead, Operations stabilized and BLDR realized synergies, net income bounced back to around 200,000 and sales growth outpaced COGS by a 40% margin. Overall, the acquisition period quickly catalyzed revenue and FCF growth, and BLDR have purchased companies at comparatively low multiples to their peers. In terms of the future, the acquisition strategy is to target companies with advancements in prefab and utilize the unique FCF leverage they have. Specifically with the BMC acquisition, management has already raised cost synergy guidance from 100m to 150m. The increase in market share allows BLDR to capitalize on favorable macro trends. An artificially low 30-year mortgage rate, pent up demand from a supply shortage, and strong SF housing starts are on the horizon. Other tailwinds include demographic changes, WFH, and a record low supply of homes.
- **Underappreciated Prefab business catalyzes future non-commodity growth:** In conventional "stick-build" construction, builders cut and assemble lumber on site. Prefabricated components are engineered in an offsite location using specialized equipment and labor. This outsourced task allows for optimal material usage, lower overall labor costs and improved quality of structural elements. In addition, using prefabricated components results in faster construction because carry a 1000 bps gross margin% premium over lumber sheet goods and 60% of homes in the U.S. currently built w/o any prefab components, so there is room to capitalize on the technology. BLDR is by far the furthest along in prefab advancements in the industry, and they are now working towards automating the prefab process, to increase efficiency. The market consensus is that the industry produces commodities. BLDR is significantly different on 2 fronts. Firstly, lumber sales have fallen to 30% of revenue, down to nearly half of its weight just 3 years ago. Secondly, the more manufactured products that BLDR prefabs, the more diversified their product offerings become, because they are providing an additional value-add service to customers. In fact, BLDR's investment in prefab is evident in their roll-up strategy, which is focused on targeting companies that specialize in prefabricating a specific building material. Buying prefab allows more value-added products to be manufactured offsite, making life easier for the homebuilder. Automating manufacturing also allows BLDR to focus on its turn-key services that increase brand loyalty, like design assistance, process management, and professional installation of products.

Key Ratios and Statistics:

Share Price (9/29/21)	$53.92
Market Cap (000's)	$11,170
Enterprise Value	$13,180
52-Week Low	$29.73
52-Week High	$55.54
Revenue (FY20)	$8,558
EBIT (FY20)	$5,438

($Mm)	**2019A**	**2020A**	**2021E**	**2022E**
Revenue:	728,043	855,874	2,057,810	2,154,330
EBITDA:	49,234	66,042	186,087	183,809
Net Income:	22,180	31,353	105,694	102,355

Figure 1 – BLDR Price Action

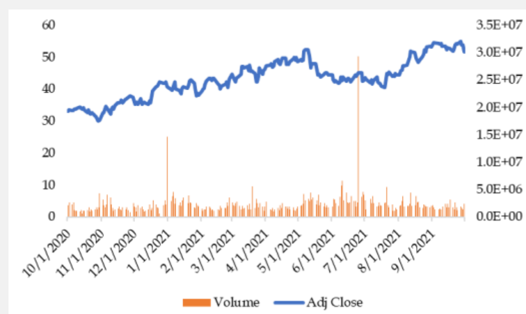


Figure 2 – BLDR ROIC History

ROIC	2017	2018	2019	2020	2021
Q1	3.17%	3.50%	5.26%	4.11%	6.80%
Q2	5.52%	5.57%	7.62%	6.56%	17.16%
Q3	5.61%	6.79%	8.39%	6.60%	
FY	**19.67%**	**24.06%**	**27.77%**	**24.86%**	

Operating Build

Income Statement - BLDR	2018	2019	2020	2021 (p)	2022 (p)	2023 (p)	2024 (p)	2025 (p)
(In Thousands, Except per share data)								
Revenue Breakdown								
Lumber & Lumber sheet goods	4,480,367	3,858,628	3,081,195	6,717,004	6,985,684	7,125,398	7,267,906	7,413,264
Manufactured Products	1,158,716	1,237,673	1,626,186	4,634,630	4,935,881	5,281,393	5,651,090	6,046,667
Windows, Doors and Millwork	1,004,220	1,164,869	1,626,186	3,984,156	4,143,522	4,350,698	4,611,740	4,934,562
Other services (Turn Key, Roofing)	1,081,468	1,019,260	2,139,719	5,242,310	5,478,214	5,642,561	5,811,838	5,986,193
Total Revenues:	**7,724,771**	**7,280,431**	**8,558,874**	**20,578,101**	**21,543,302**	**22,400,050**	**23,342,574**	**24,380,686**
Cost of Sales:	5,801,831	5,303,602	6,336,290	15,022,014	15,618,894	16,128,036	16,573,228	17,066,480
Gross Margin	**1,922,940**	**1,976,829**	**2,222,584**	**5,556,087**	**5,924,408**	**6,272,014**	**6,769,347**	**7,314,206**
Merger Synergies	-	-	-	50,000	50,000	50,000	-	-
SGA:	1,553,972	1,584,523	1,678,730	4,115,620	4,524,093	4,704,011	4,901,941	5,119,944
EBIT:	**368,968**	**392,306**	**543,854**	**1,490,467**	**1,450,315**	**1,618,004**	**1,867,406**	**2,194,262**
Interest Expense	108,213	109,551	135,688	117,817	121,019	124,841	121,226	122,362
EBT	**260,755**	**282,755**	**408,166**	**1,372,650**	**1,329,296**	**1,493,162**	**1,746,180**	**2,071,900**
Tax Expense	55,564	60,946	94,629	315,709	305,738	343,427	401,621	476,537
Net Income	**205,191**	**221,809**	**313,537**	**1,056,940**	**1,023,558**	**1,149,735**	**1,344,559**	**1,595,363**

Drivers - BLDR								
Lumber & Lumber sheet goods growth		*-13.9%*	*-20.1%*	*118.0%*	*4.0%*	*2.0%*	*2.0%*	*2.0%*
Manufactured Products growth		*6.8%*	*31.4%*	*185.0%*	*6.5%*	*7.0%*	*7.0%*	*7.0%*
Windows Doors and Millwork growth		*16.0%*	*39.6%*	*145.0%*	*4.0%*	*5.0%*	*6.0%*	*7.0%*
Other services growth		*-5.8%*	*109.9%*	*145.0%*	*4.5%*	*3.0%*	*3.0%*	*3.0%*
Total Revenue growth		*-5.8%*	*17.6%*	*140.4%*	*4.7%*	*4.0%*	*4.2%*	*4.4%*
Cost of sales % Revenue	*75.1%*	*72.8%*	*74.0%*	*73.0%*	*72.5%*	*72.0%*	*71.0%*	*70.0%*
Gross Margin % Revenue	*24.9%*	*27.2%*	*26.0%*	*27.0%*	*27.5%*	*28.0%*	*29.0%*	*30.0%*
SGA % Revenue	*20.1%*	*21.8%*	*19.6%*	*20.0%*	*21.0%*	*21.0%*	*21.0%*	*21.0%*
EBIT % Revenue	*4.8%*	*5.4%*	*6.4%*	*7.2%*	*6.7%*	*7.2%*	*8.0%*	*9.0%*
Interest Expense % Revenue	*1.4%*	*1.5%*	*1.6%*	*0.6%*	*0.6%*	*0.6%*	*0.5%*	*0.5%*
Tax Expense % Revenue	*21.3%*	*21.6%*	*23.2%*	*23.0%*	*23.0%*	*23.0%*	*23.0%*	*23.0%*

Valuation

Discounted Cash Flow - Unlevered Free Cash Flow						
(In thousands)	**2021**	**2022**	**2023**	**2024**	**2025**	**TV**
EBIT	1,490,467	1,450,315	1,618,004	1,867,406	2,194,262	
Tax Expense	(315,709)	(305,738)	(343,427)	(401,621)	(476,537)	
NOPAT	1,174,758	1,144,577	1,274,576	1,465,785	1,717,725	
D&A	370,406	387,779	403,201	420,166	438,852	
Cap EX	(329,250)	(344,693)	(358,401)	(373,481)	(390,091)	
Changes in NWC	863,035	63,270	53,895	46,696	51,751	
Free Cash Flow	352,879	1,124,394	1,265,481	1,465,773	1,714,735	**22,585,396**
Discounted Free Cash Flow	319,979	924,504	943,499	990,941	1,051,170	13,845,348

WACC Table	
Equity %	73.00%
Debt %	27.00%
Risk Free Rate	1.31%
Levered beta	2.41
ERP	4.38%
Cost of equity	11.87%
Cost of debt	6.00%
Calculated WACC	10.28%
WACC Used	10.28%

Valuation		
Terminal Growth		2.50%
Implied Multiple		8.58
EV		18,075,441.17
Net Debt		1,953,551.00
Equity Val		16,121,890.17
S/O		207,830.00
Target Price	**$**	**77.57**
Current price	$	54.12
Implied Upside:		**43.33%**

Sensitizing Terminal Growth and WACC

		Weighted Average Cost of Capital				
	43.334%	8%	9.00%	10.00%	11.00%	12.00%
TV Growth Rate	1%	73%	47%	27%	11%	-2%
	1.50%	85%	56%	34%	16%	2%
	2.00%	99%	66%	41%	22%	7%
	2.50%	116%	78%	50%	29%	12%
	3.00%	137%	92%	60%	36%	17%
	3.50%	162%	108%	71%	44%	24%
	4.00%	193%	128%	85%	54%	31%

Precedent Transactions

Date	Acquiror	Target	EV / EBITDA
January 2021	Builders FirstSource, Inc.	BMC Stock Holdings, Inc	7.3x
August 2020	Clayton, Dubilier & Rice	HD Supply Holdings, Inc.'s Construction & Industrial	9.0x
May 2018	Reece Limited	Morsco Inc.	14.4x
April 2018	GMS Inc.	WSB Titan	9.2x
August 2017	Beacon Roofing Supply, Inc.	Allied Building Products Corp.	13.6x
June 2017	Clayton, Dubilier & Rice	HD Supply Holdings, Inc.'s, Waterworks Business	10.5x
August 2016	ABC Supply Co., Inc.	L&W Supply	12.9x
July 2015	Beacon Roofing Supply, Inc.	Roofing Supply Group	14.6x
July 2015	The Home Depot, Inc.	Interline Brands, Inc.	11.1x
June 2015	Stock Building Supply Holdings, Inc.	Building Materials Holding Corporation	11.4x
April 2015	Builders FirstSource, Inc.	ProBuild Holdings LLC	9.6x
May 2014	CCMP Capital Advisors, LLC	The Hillman Companies, Inc.	11.7x
February 2014	AEA Investors	Gypsum Management & Supply, Inc.	10.0x
May 2012	GS Capital Partners and P2 Capital Partners	Interline Brands, Inc.	9.7x
September 2010	Hellman & Friedman	Associated Materials Incorporated	9.0x
April 2010	Oak Hill Capital Partners	The Hillman Companies, Inc.	10.0x
June 2007	Bain, Carlyle Group & Clayton, Dubilier & Rice	HD Supply Holdings, Inc.	8.5x

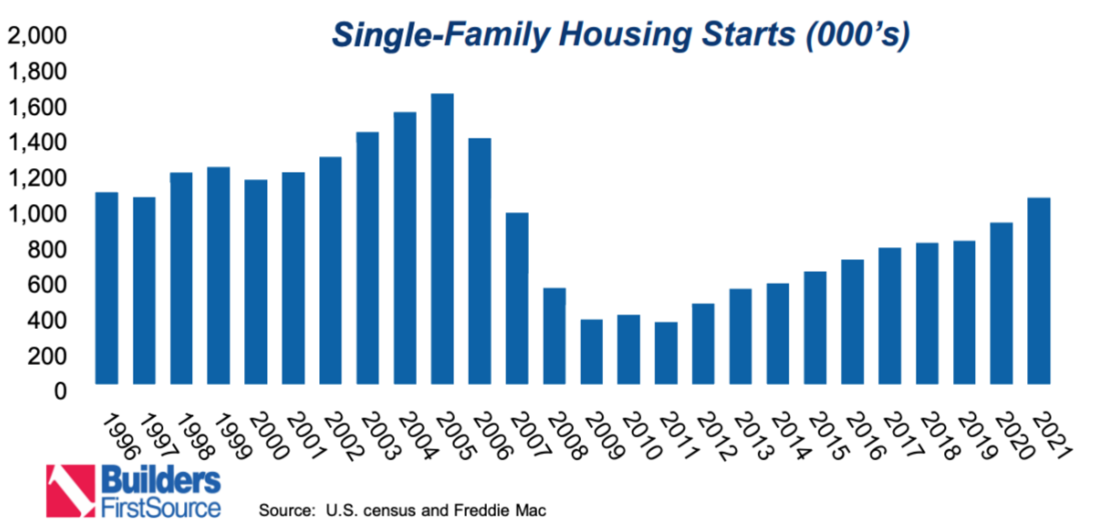
Mean	11.0x
Median	10.5x

Comparable Company Analysis

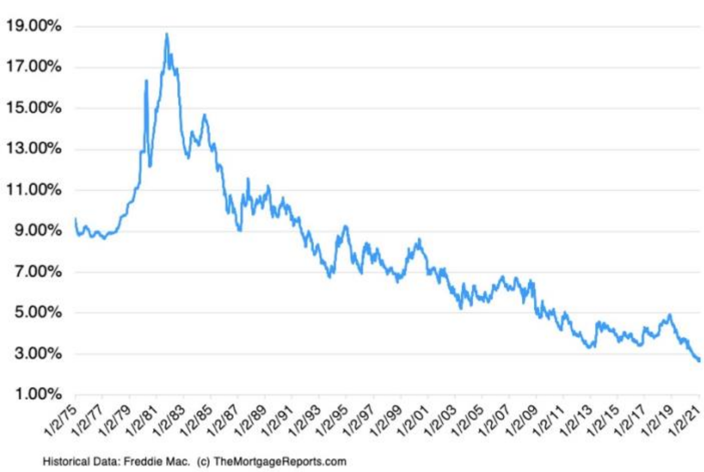
BLDR Comp Set Company Name	Enterprise Value	EV/LTM EBITDA	LTM EBITDA Margin	Net Debt/EBITDA	EBITDA, 1 Yr Growth	ROIC (Annualized)	Revenues, 1 Yr Growth
Beacon Roofing	5,870.0	9.92x	8.8%	3.1x	14.00%	14.04%	2.74%
Bluelinx Holdings	1,250.0	7.80x	9.0%	1.7x	19.00%	18.52%	13.00%
UFP Industries	4,984.0	7.50x	8.9%	1.0x	21.00%	19.94%	16.50%
Cavco Industries,	1,940.0	16.50x	9.1%	0.2x	15.80%	22.68%	12.50%
GMS Inc (NYSE:	3,233.0	9.08x	9.8%	3.5x	14.25%	16.90%	10.70%
Masonite Worldwide (NYSE:	3,430.0	10.12x	12.0%	2.8x	2.40%	15.80%	4.80%
Builders	13,130.0	8.19x	11.6%	1.5x	61.00%	24.86%	38.76%

Summary Statistics	Enterprise Value	EV/Forward EBITDA	LTM EBITDA Margin	Net Debt/EBITDA	EBITDA, 1 Yr Growth	ROIC (Annualized)	Revenues, 1 Yr Growth
High	13,130.0	16.50x	12.0%	3.5x	61.00%	24.86%	38.76%
Low	1,250.0	7.50x	8.8%	0.2x	2.40%	14.04%	2.74%
Mean	4,833.9	9.87x	9.9%	2.0x	21.06%	18.96%	14.14%
Median	3,430.0	9.08x	9.1%	1.7x	15.80%	18.52%	12.50%

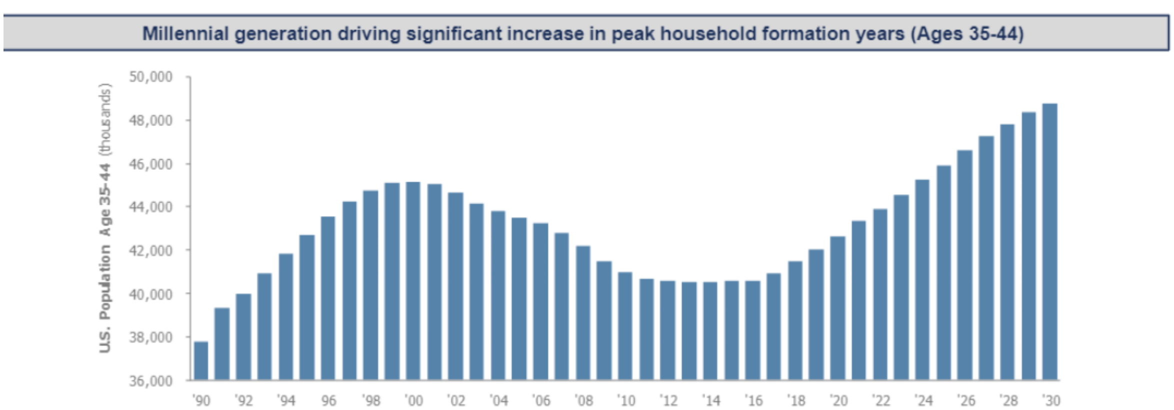
SF Housing Start Growth



30 Year Mortgage Rate



Demographic Flip



Flex Ltd. (NASDAQ: FLEX)

A cheap EMS pick amid operational improvements, industry rationalization, and a hidden solar asset

Rhys Berezny
Junior Analyst
rhys.berezny@stern.nyu.edu

Sector: Technology **October 1st, 2021**

Business Description:

Flex Ltd. is a leading global electronic manufacturing services company and provides design, engineering, manufacturing, and supply chain services to original equipment manufacturers (OEMs). The revenue segments are reported as Flex Agility Solutions (FAS) and Flex Reliability Solutions (FRS). FAS consists of consumer, lifestyle and communication electronics contracts which are heavily commoditized. These contracts are cyclical, short-term (6-12 months), very low margin, and generally unattractive. FRS consists of contracts for automotive, healthcare, and industrial end markets which require greater technological expertise and are much more regulated. Contracts in this segment are long-term (5-10 years) and sticky making this segment command a valuation premium compared to FAS. NEXTracker, the solar tracker company acquired by Flex in 2015 is included within the FRS segment.

Investment Thesis:

New Management, New Vision: Flex is much stronger business than it used to be in part due to its new management. After a failed and costly venture with Nike and the sudden retirement of its CEO, Flex had a fresh start, hiring Revathi Advaithi as the new CEO in 2019 and Paul Lundstrom as CFO in 2020. In just one year, Flex eliminated $1.2B of poor margin business by pruning its portfolio of low-quality contracts on the Agility side and only pursuing contracts that meet stringent ROIC and cash generation hurdles. Since Revathi came in, Flex has focused on developing its strengths, primarily in its Reliability segment. Flex has improved their FAS-FRS mix from 63%-37% to 54%-46% in two years.

Industry Rationalization: EMS players are shedding commoditized contracts and mindless revenue growth. "Empire-builder" executives have exited the industry, and these players now heavily favor stability and ROIC. Major comparable companies like Celestica and Plexus have shed major low margin contracts in the commoditized market, even with significant dips in revenue, demonstrating the industry's increasing sensibility. Even with many top-quality EMS companies now targeting regulated end-markets, the market is far from saturated as OEMs continue to outsource their work. Over time, margin expansion in the industry could lead to a multiple rerate for these top companies.

Growing FRS Segment: Flex's Reliability segment is the growth engine of the company. FRS takes time to establish relationships and get approvals with large OEM's, yielding recurring, stable business. The automotive and healthcare verticals are major drivers for long-term margin expansion for Flex due to the specialization required to produce these products. Flex currently has a major $400MM annual revenue contract in Buffalo Grove to produce glucose monitors that will drive 20%+ gross margin, 5%+ run rate growth for years to come. In the automotive sector, Flex is at the forefront autonomous and EV electronics design and will benefit from being one of the first EMS' part of this secular growth.

Value Potential through NEXTracker: In 2015, Flex acquired NEXTracker for $330MM. NEXTracker builds solar trackers that automatically tilt solar panels towards the sun. NEXTracker is now a market leader in the solar tracker industry with annual revenues of around $1B and double-digit operating margins. The market ascribes minimal value to this asset and management is actively pursuing a spin-off; Flex confidentially filed an S-1 in April. I value it at around $2.5B using sales multiples for Array Technology, a highly comparable solar tracker firm. Even without a spin-off in the near future, NEXTracker is a solid business and provides a steady and strong cash flow to Flex.

Key Ratios and Statistics:

Price Target	$31.22
Expected 3-year IRR	25.9%
Share Price (10/01/21)	$18.57
Market Cap	$9.07B
Average Daily Volume	2.97M
52-Week Low	$10.86
52-Week High	$20.04
Cash	$2.69B
Total Debt	$3.78B
Forward P/E	10.13x

Segment	Sales	EBIT %	2-yr Growth
FAS	$13.5B	2.26%	-19.9%
FRS	$9.4B	4.04%	12.1%
NEXT	$1.2B	14.34%	27.5%

Figure 1 – Stock Performance - Last 5 Years

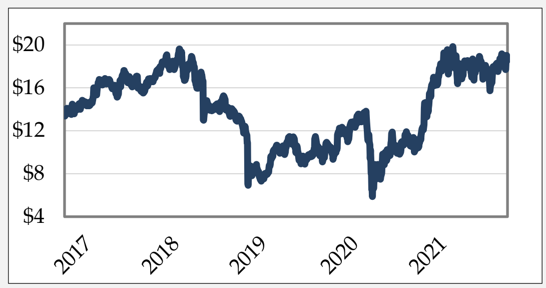
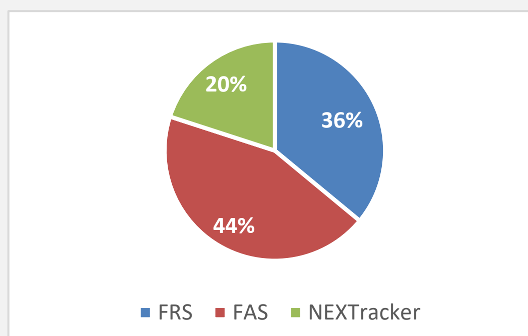


Figure 2 – % of Total EBIT By Segment



Executive Summary

Flex is not a business that investors have historically gravitated towards. Flex has typically returned razor-thin, low to mid-single-digit operating margins while constantly competing with other EMS providers for low-quality contracts. However, Flex has begun turning itself around in the last two years by sorting out some key operational issues while remaining very cheap. I believe that Flex is in a far better situation than they have been historically due to significant operational and management decisions, whole industry rationalization, a growing higher-margin segment, and to add a cherry on top, the performance of NEXTracker, a solar tracker company that has significant standalone value and cash returns. With a 3-year projected IRR of 26%, I recommend Flex as a STRONG BUY.

Segment Overview

In Q1 2021, Flex made significant changes to its organizational structure to drive growth and efficiency while also making several accounting changes. The revenue segments are now reported as Flex Agility Solutions (FAS) and Flex Reliability Solutions (FRS).

<u>Flex Agility Solutions (56% of revenue):</u> FAS consists of high output, more cyclical product contracts that are easily scalable and have a short product lifestyle. These are mainly short-term 6–12-month contracts with lower EBIT margins (~3%) and require ongoing searching for new contracts. It includes the following sub-segments: Communications, Enterprise, and Cloud (CEC), Lifestyle, and Consumer Devices.

<u>Flex Reliability Solutions (44% of revenue):</u> FRS consists of higher quality, more regulated product contracts, which require complex technology and greater expertise. These are long-term, multi-year contracts with higher operating margins. It includes the following sub-segments: Automotive, Health Solutions, and Industrial. NEXTracker, the solar tracker company acquired by Flex in 2015, is included within the Industrial subsegment.

Industry Overview

The global electronic contract manufacturing and design services industry was valued at $417B in 2019 and is expected to grow by an estimated 8.5% CAGR from 2020 to 2027 to an industry size of $800B. EMS contracts can be made at any point during the production process. This process is highly individualized, and EMS companies can provide services as simple as assembly, component sourcing, testing, or more complex solutions, including design, component manufacturing, and prototype assembly. These services are driven by an EMS company's ability to specialize in economies of scale, industrial design expertise, raw materials procurement, along with value-added services. It allows OEMs (buyers) to avoid tedious or complex large operations and outsource this work to reduce costs as well as time-to-market production. They can allocate more of their time and effort on R&D, marketing, and sales. As electronics' technology rapidly advances, competition in the electronics markets increases, forcing OEMs to outsource more of their work to provide more business to EMS players.

New Management

Flex is a more robust business across all facets than it was just two years ago. New management has been part of this positive change. After a failed partnership with Nike to improve Nike's manufacturing supply chain in Mexico in 2018, along with disappointing earnings and the sudden "retirement" of Flex's CEO, Mike McNamara, Flex's share price plummeted 50%. In February 2019, Revathi Advaithi joined Flex after working as president and COO for Eaton's Electrical Sector, a $13B operation. After joining Flex, she instituted a turnaround plan to improve margins, change existing contracts, and raise free cash flow by improving core company operations.

Revathi helped Flex reorient its approach to focus on growth opportunities that drive margin expansion instead of revenue growth. Flex eliminated $1.2B of poor margin business by pruning the portfolio of low-quality contracts on the Agility side and focusing on high-growth end markets. These losses in revenue were in-part replaced by more lucrative long-term contracts for the automotive, industrial, and medical sectors driving up margins. The mix between Agility and Reliability segments changed from 63% and 37% to 54% and 46% in just two years.

Through trade wars and a global pandemic, Flex's robust supply chain network allowed for solid returns. Elevated freight costs in Q4 and the most recent Q1 posed a threat for lower margins; however, Flex returned a substantial 20% ROIC and increased its earnings targets for next year. These superior results are likely a testament to the new changes imposed by new leadership. As the contract mix continues to shift and operations become more and more efficient, we are likely to see increased revenues in high-margin segments that are accretive to FCF and overall margins. All segments in Flex are now moving in the direction of solid organic growth.

Flex has outperformed EPS expectations in the last three quarters by 20-40%. Yet, the share price has been flat, indicating an uncertainty among investors which could be in part due to the prior management's failure to execute. However, for the reasons above, I believe management has Flex on the right track and will not downgrade guidance.

Industry Rationalization

Flex has not been the only company to make changes across the board. The age of immense price competition, endless revenue growth, and low margins are on the decline. Across the industry, the higher-quality firms have moved away from commoditized manufacturing and are getting into more regulated markets, as competition with many Asian firms like Foxconn is extremely tough, especially when your company has much lower market share/power. This shift to regulated markets has led to better margins, higher ROICs, and more stable and predictable earnings. Over time, these companies have expanded their focus from just supply chain efficiency, cost-minimization, and high utilization. Now, these companies are often a part of the entire product life cycle and leverage their technical expertise and specialization to establish strong, long-term relationships with OEMs.

Flex isn't the only mover and shaker. Celestica, a Canadian EMS company, disengaged with several Cisco contracts, causing a 10% reduction in revenue. Plexus, a very high-quality EMS player, has reduced its communication segment from 20% of total revenues to mid-single digits in just over a year. Additionally, there has been very significant management turnover across the industry for companies who had wanted revenue growth for purely growth's sake. These changes in strategic objectives in the last couple of years are a testament to the new focus of quality over quantity, lower competition, and increased sensibility in the EMS space. With time, these changes could lead to a multiple rerate for top performers in the EMS industry.

Reliability Growth

The Reliability segment is the real focus for this business. The key advantage to the Reliability segment is that the contracts do not shift around much from company to company, and relationships with OEMs are very sticky and long-term, which lends itself to higher margins. Currently, the best performing EMS industry is Plexus since most of its contracts are in highly regulated verticals. I believe FRS deserves a similar EBITA multiple of 13-14x, given its similar contract composition.

The TAM for high-quality EMS providers is estimated to be around $100B and is rapidly growing. Currently, 70% of manufacturing (and quickly shrinking) is done in-house at the OEMs, leaving a lot of room for market growth. Regulated industries have historically not favored outsourcing to the EMS providers, but given the increasing technological capabilities of EMS companies, OEMs have begun to change their tune. Additionally, an increased focus on design work (FRS represents 70% of Flex's design work) and supply chain solutions has increased the value-add of certain EMS companies like Flex. Vertical tailwinds in the FRS subsegments that will contribute to revenue growth and margin expansion can be found below.

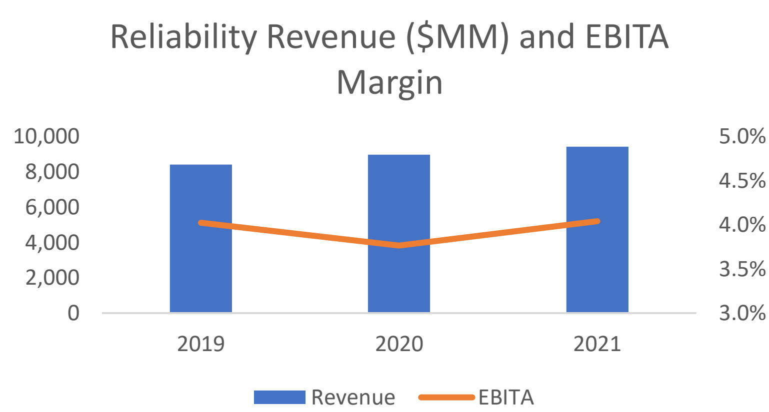
FRS Vertical Explanations

<u>Healthcare (~$2B revenue, HSD EBITA, 10% growth):</u>

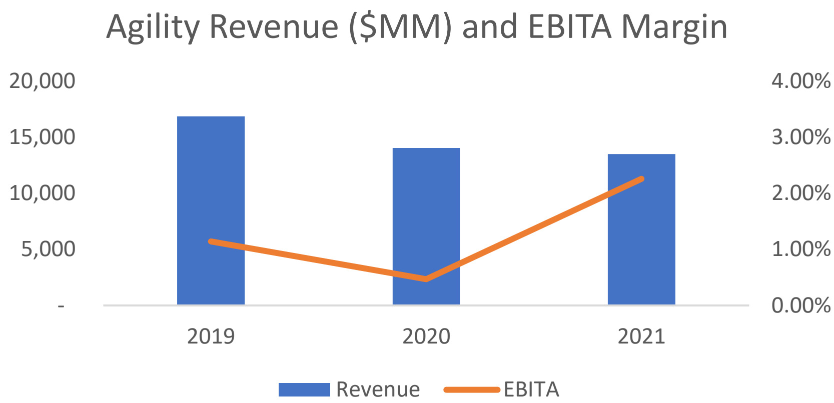
The healthcare segment is characterized by very long and stable contracts. Many of the manufactured devices require FDA approval which must be recertified if the manufacturer/process changes, making these contracts very sticky. It is unacceptable for there to be a product flaw due to the nature of the industry, and so high-quality EMS companies are necessary. These contracts are the most difficult to break into, but once acquired, they provide the highest margins and are the least cyclical business segment. Flex has recently secured contracts for higher-growth drug delivery products and other cutting-edge medicine technology contracts to build credibility for these niche devices. Flex currently has a major $400MM annual revenue contract in Buffalo Grove to produce glucose monitors that will drive 20%+ gross margin and 5%+ run rate growth for years to come. Many OEMs including, Philips, Abbott, and Johnson and Johnson are gradually outsourcing more of their manufacturing and design processes to regional US companies creating more potential contracts for Flex.

<u>Automotive (~$3B revenue, HSD EBITA, 8% growth):</u>
Although the automotive segment has historically been quite commoditized, there is now great potential within the industry. Flex splits its revenues 1/3 contract manufacturing, 1/3 joint design and 1/3 full product technology, which Flex owns the IP for. This enables Flex to achieve higher margins than traditional EMS companies. Flex focuses on autonomous, connectivity, electrification, and smart tech. These are major growth areas within the automotive sector due to the push for EV and AV vehicles; EV's have a projected CAGR of 20% until 2030. As these cars become more complicated, they also command increasingly complex sensors and electronic systems, which bodes very well for EMS providers. Over the next ten years, semiconductor components' total cost (which are very highly correlated with electronics parts) per autonomous car will increase by around 5x, according to NXP Semiconductors. This is beneficial for higher-tier EMS companies like Flex, who will win these lucrative contracts due their existing relationships and expertise. However, this sector is the most cyclical segment within FRS and has been hit by the chip shortage.

<u>Industrial (~$4B revenue ex NEXTracker, MSD EBITA, 7% growth):</u>
Flex focuses on capital equipment, industrial devices, renewable and grid technology, and power systems within the Industrial segment. These make up around 35% of FRS's revenue (ex NEXTracker) and have been a driving force behind Flex's recent margin expansion. Although industrial is less of a growth area than the previous two segments, specific contracts within industrial including capital equipment manufacturing, provide solid margins but are subject to cyclicality. There are some growth elements within Industrial such as next-generation robotics, but these innovations are still in early stages.



A Quick Note on Agility
Agility (12B revenue, 3% EBIT, 3% growth):
This business line is nowhere near as attractive as FRS and will likely grow at GDP levels in the near future. Drivers including 5G rollout with major customers, including Nokia and Ericson, and a large, new design contract with Dyson may improve margins. As stated earlier, Flex cut $1.2B of low-quality contracts and is now only pursuing contracts that meet stringent ROIC and cash generation hurdles, which has made FAS a slightly better business. Management is focusing on increasing the quality, not quantity, of these contracts, but it is unlikely revenue will continue to decline. This segment should be valued along with the industry average at around 8-9x EBITA.



NEXTracker

In 2015, Flex acquired NEXTracker for $330MM as one of the many pet projects that the former CEO pursued. NEXTracker makes solar trackers that automatically orient solar panels toward the sun, increasing the energy the panels generate. NEXTracker is a market leader in the solar tracker industry with annual revenues of around $1B and double-digit operating margins. With the push towards more renewable energy and a more carbon-neutral economy, solar projects are supposed to increase dramatically; NEXTracker is heavily levered towards industrial solar project growth. The five-year CAGR for solar trackers is forecasted at around 11-15%. Unlike its peers, NEXTracker maintains good hedging practices for commodity inflation. Its supply chain and current relationship with Flex allow it to pass on its costs, allowing it to weather some short-term difficulties. In addition, NEXTracker has proven itself as a reliable and quality product in an emerging industry. Given this, NEXTracker's revenue growth will likely at least meet industry growth over the next five years and continue earning double-digit operating margins.

On April 28, Flex released a statement announcing that they confidentially filed an S-1. Management believes Flex is not receiving sufficient value for this asset and is actively pursuing a spin-off; however, there is no information on the deal composition or specific timing. A key KPI for NEXTracker is the company, Array Technologies. They have comparable sales, operating margins, and growth prospects to NEXTracker. As Array's current market cap is around $2.3B, it is safe to say NEXTracker is currently worth roughly that amount, if not slightly more. Management will likely wait until capital markets for this industry improve, especially as Array has dropped 60% in value since the start of the year due to high input costs and overstated earnings guidance. The NEXTracker spin-off will be a strong value-generating transaction for shareholders. Management is likely to buy back shares with the proceeds as it aligns with Flex's objective and goals. They have historically returned 50% of FCF to shareholders in the form of buybacks. Flex has recently stated that they are open to strategic acquisitions but would only go this route if they believe they are getting it for cheap.

The extreme upside case would be for Array to return to near previous levels of roughly $5B, and therefore NEXTracker would spin at a similar price point, although this case is not likely. Even if NEXTracker is not spun off in the short-medium term, it still is a solid business that provides a steady and strong cash flow to Flex. In my model, I conservatively projected NEXTracker as its own line, and even on that basis, it is very quick cheap and does not seem to be factored into the Flex's current price.

Comparable Company Analysis

P/E	2015	2016	2017	2018	2019	2020	LTM
Flex	15.11	27.67	17.29	55.05	56.15	14.27	11.27
Plexus	13.22	22.42	18.27	144.77	20.21	18.19	17.09
Jabil	15.37	15.87	38.06	45.03	19.47	97.37	14.49
Sanmina	4.85	12.34	17.61	-18.21	14.85	14.99	9.19
Celestica	16.39	9.97	9.82	14.20	18.53	19.43	14.94

EV/EBITA (ex. unusual)	2015	2016	2017	2018	2019	2020	LTM
Flex	11.30	14.12	13.75	10.49	8.88	10.43	8.84
Plexus	9.43	13.09	13.18	14.69	15.94	13.53	13.06
Jabil	8.35	9.32	9.81	8.39	9.03	9.40	9.11
Sanmina	9.16	12.04	10.64	10.46	7.61	7.73	6.31
Celestica	8.45	7.95	6.70	9.42	11.60	9.17	9.05

EV/EBITA (in. unusual)	2015	2016	2017	2018	2019	2020	LTM
Flex	12.98	17.88	12.27	16.20	18.04	11.44	9.48
Plexus	9.58	15.09	13.16	14.64	16.17	14.06	13.35
Jabil	8.82	9.54	13.53	9.18	10.50	14.73	10.66
Sanmina	9.62	12.14	10.73	15.43	7.97	8.95	6.66
Celestica	10.90	8.88	8.33	14.93	8.28	8.74	8.36

EV/EBIT (ex. unusual)	2015	2016	2017	2018	2019	2020	LTM
Flex	12.45	15.94	15.67	11.90	9.73	11.10	9.33
Plexus	9.43	13.09	13.18	14.83	16.08	13.63	13.15
Jabil	8.68	9.79	10.44	8.95	9.42	10.13	9.50
Sanmina	9.26	12.22	10.64	10.46	7.61	7.73	6.31
Celestica	8.97	8.19	6.91	9.42	14.45	10.82	10.34

EV/EBITDA (ex. unusual)	2015	2016	2017	2018	2019	2020	LTM
Flex	6.92	8.77	8.22	6.18	5.64	7.37	6.54
Plexus	6.76	9.34	9.90	10.58	11.75	10.05	9.93
Jabil	4.59	4.27	4.41	3.82	4.63	4.50	5.20
Sanmina	6.26	8.24	7.08	6.37	5.43	5.41	4.81
Celestica	6.18	5.97	4.91	6.16	6.28	5.41	5.55

Valuation

USD mm CY	2018	2019	2020	2021E	2022E	2023E
Earnings Model						
x **Segment Breakdown**						
FAS						
Sales	16,855	14,053	13,493	14,168	14,593	14,957
Income	442	369	449	496	511	598
EBITA	193	66	305	299	307	390
FRS						
Sales	8,415	8,981	9,431	9,997	10,697	11,445
Income	463	532	482	550	642	801
EBITA	339	338	381	411	493	642
NEXTracker						
Sales	941	1,176	1,200	1,380	1,546	1,700
Income	71	110	180	124	170	170
EBITA	65	101	172	115	160	159
Unallocated Expenses						
Corporate and Other	(104)	(113)	(80)	(89.41)	(93.92)	(98.36)
Stock-based Compensation	(76)	(71)	(79)	(76.63)	(80.50)	(84.31)
Impairment	(87)	(106)	7	(76.63)	(80.50)	(84.31)
Restructuring charges	(113)	(216)	(101)	(102.18)	(107.34)	(112.41)
Legacy allocated cost	(374)	(497)	(245)	(336)	(352)	(368)
Legacy Revenue	25,270	23,034	22,924	24,165	25,289	26,403
Total Revenue	**26,211**	**24,210**	**24,124**	**25,545**	**26,835**	**28,103**
Total Income	**976**	**1,011**	**1,111**	**1,170**	**1,323**	**1,569**
Legacy EBITA	**531**	**404**	**686**	**710**	**800**	**1,031**
Nextracker EBITA	**65**	**101**	**172**	**115**	**160**	**159**
Total EBITA	**596**	**505**	**858**	**825**	**960**	**1,190**

Sum of the Parts	**FAS**	**FRS**	**Nextracker**
2023 EBITA	390	642	159
Multiple	8.99x	14.07x	15.25x
EV	3,501	9,028	2,424
Total EV	14,953		
Combined Multiple	12.56x		

Valuation		**Return Stream**	**9/30/2021**	**12/31/2021**	**12/31/2022**	**12/31/2023**
EV	14,953	Dividend/share		-	-	-
(-) Net Debt - Assets	554	Cap Gain	(18.57)	-	-	31.22
Equity Value	14,399	Cash Flow	(18.57)	-	-	31.22
Per Share	31.22	IRR	25.94%			
Price Today	18.57					
EV Today	10,932	EV Out-Year	14,953		% Change	36.79%
Sales	24,124	Sales	28,103		% Change	16.49%
Margin	3.56%	Margin	4.2%		Expansion	0.68%
EBITA	858	EBITA	1,190		% Change	38.71%
Multiple	12.74x	Multiple	12.56x		Expansion	-0.18x
Net Debt - Assets	1,870	Net Debt - Assets	554		De-levering	(1,315)
Shares Outstanding	488	Shares Outstanding	461		Share Delta	(27)
Price	18.57	**Price**	**31.22**		**% Change**	**68.10%**