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INVESTMENT STRATEGY OUTLOOK – INTERNATIONAL EQUITY

March 31, 2020

The first quarter of 2020 was unprecedented. The Coronavirus (COVID-19) pandemic took the world by storm, rapidly spreading fear and panic across the globe. Stock markets collapsed in just a few short weeks as governments ordered their citizens to “shelter in place,” shutting down huge swaths of the economy in the name of public safety. Thousands of lives were tragically lost to the virus, millions of jobs disappeared, and businesses were left wondering whether they would be able to meet their obligations as revenue evaporated. Facing a global economic recession, governments and central banks launched aggressive economic rescue packages. This included extraordinary stimulus, quantitative easing (QE) and interest rate cuts, among other measures. While the full story is yet to be written, great uncertainty remains as we pen this letter.

Equity valuations were stretched well before COVID-19. At the same time, economic and business fundamentals had been deteriorating, with companies piling on debt through aggressive mergers & acquisitions and share buybacks, in lieu of organic capital investment. In our view, stock markets were already fragile, and COVID-19 sent them over the edge. As we mentioned in our June 2018 letter, we were often being asked what we think will cause the next bear market, and we wrote, “Our advice would be to expect the unexpected, as there’s a good chance that the next bear market will be driven by catalysts that no one sees coming.” As we are witnessing today, external shocks can be difficult to digest and extremely disruptive. It’s safe to say that COVID-19 was not on anyone’s radar, and it will take some time before the dust settles.

At this early stage, COVID-19 has hurt value investors much more than their growth counterparts. Many sectors and industries in the value camp, such as financials, energy, industrials, travel and hospitality, have been the hardest hit by the virus. Intensifying the market pressure, Saudi Arabia’s unexpected move to open the spigots has crushed the price of oil. Nearly all energy-related companies, including businesses that only have moderate energy exposure, have seen their stocks decline precipitously. Year-to-date, value has underperformed growth by 10.69%, as the MSCI EAFE Value Index has declined 28.20%, while the MSCI EAFE Growth Index fell by only 17.51%. Over the last 12 months the gap is even wider, at a remarkable 16.92% differential. There is seemingly no price too high for defensive or growth companies, and no price too low for cyclical or out-of-favor value names.

Given the backdrop and FMI’s value orientation, it’s been a frustrating start to the year. In the quarter, the FMI International portfolios declined by approximately 28.1% (currency hedged) and 29.1% (unhedged), respectively, which compares with an MSCI EAFE Index decline of 20.55% in local currency (LOC) and 22.83% in U.S. Dollars (USD). Finance (underweight) and Transportation sectors, as well as a lack of direct exposure to Energy Minerals were positive contributors to the portfolio’s relative performance, while Consumer Services (travel and hospitality), Health Technology, and Industrial Services dragged down the results. Unilever, Samsung Electronics, and Sony performed well on a relative basis, as Schlumberger, WPP, and CNH Industrial detracted. An underweight allocation to Japan also hurt, as Japan has been far less impacted by COVID-19 than its European peers thus far. A strengthening U.S. Dollar was a tailwind for the hedged strategy.

Encouragingly, today many stocks are attractive in an absolute sense, not just on a relative basis. There is a lot of macro uncertainty, but ultimately COVID-19 is likely to be a temporary setback. While we expect a lot of volatility over the next few quarters, if investors have a long-term time horizon, we believe the risk versus reward remains compelling. Fear and human emotion have played a meaningful role in the stock market selloff, which has been exacerbated by low liquidity, algorithmic trading and passive investing. Although stock prices have fallen dramatically, the underlying businesses in the portfolios are resilient. In most cases, the stock price declines are overdone. It’s important to remember that stock prices are just a temporary mark-to-market, and the current disconnect between price and underlying business value, if history serves us, *will* rectify itself over time.

The FMI International portfolios own a collection of high-quality, durable businesses that we expect to weather the storm. Our high-quality companies are well-run, have strong balance sheets (which is especially important in the current environment), and trade at a significant discount to the market and their intrinsic values. This should be a winning combination over the long term. We increased our personal investments in the FMI International portfolios during the quarter.

COVID-19 Aftermath

By the time this letter is read we will have a much greater understanding of COVID-19, so it is hazardous to make too many definitive statements now. On the optimistic front, it appears that the ultimate mortality rate is likely to be lower than some of the figures reported in early March. With antibody testing just beginning as of the date of this writing (March 31), we will start to gain a better understanding in a few weeks of how prevalent the infection is and how to structure a more optimal treatment and quarantine regimen.

What has been most unusual in this crisis is the response. We have not seen anything quite like it in peacetime. Implementing "shelter in place" orders and shutting down large parts of major economies may be the best approach, but it is not the only option, and is not shared by all highly-respected experts or countries. It forces a set of trade-offs that perhaps people have not fully considered. This is not the place to debate something that has already been decided and is unlikely to be reversed. Investors must deal in realities. What we know for sure is that the response to this crisis will put many economies in a deep recession with substantial unemployment, and leaders are trying to cushion the blow. That said, with massive stimulus comes massive borrowing. All this debt (as well as increased corporate borrowing) will be a headwind to long-term growth. Combining the fiscal picture with central bankers' seemingly endless quantitative easing and other accommodations poses an enormous challenge down the road…

In the meantime, there is the short and intermediate term to consider. What will an economic "restart" actually look like? Will people act normally? We have already seen cancellations of many things into August. When will all the sporting events, concerts, and conferences return? We think it will take some time. Earnings for the hardest-hit industries and many cyclicals will decline significantly and are unlikely to recover soon. We believe most of these concerns are already in the stocks. Predicting people's fears and behaviors, however, is difficult. Second order effects will be widespread, hurting earnings across a very broad spectrum of sectors. Few companies will be spared. Balance sheet strength will be critical throughout the intermediate term, even with government assistance. Speculative growth stocks often rely on equity financing, which can turn fickle when fear arises. Corporate borrowing spreads, particularly in the sub-investment-grade area, have blown out in recent weeks. The cost of capital has changed dramatically over the past month.

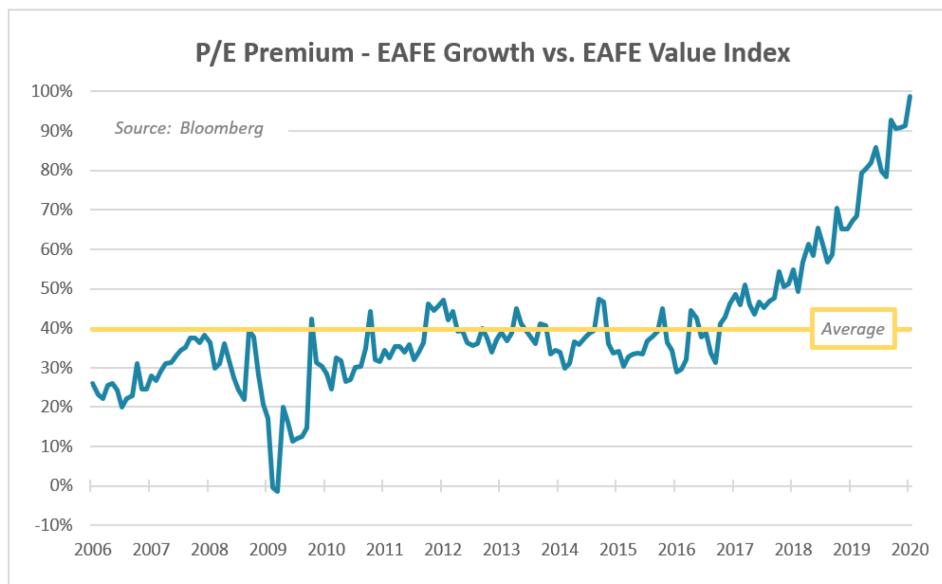
This type of environment should work in our favor. The FMI International strategies have portfolios of financially strong enterprises. We are confident in their abilities to weather a longer-than-expected recession. Value stocks should regain their multiples as the economy stabilizes. As a rule of thumb, we are using 2019 earnings as a peak to which we think most companies will return by roughly 2023, give or take a year. Some firms will recover more quickly, but our experience is that recoveries generally take longer than expected. Still, we think valuations largely incorporate these worries. Volatility is extreme, so investors must focus a few years out, rather than on the day-to-day.

Valuation Will Matter, Eventually

While many of the winning growth stocks of today are good companies, it does not mean they will be great investments going forward. Valuations for growth companies remain elevated, as are the lofty expectations for future revenue and earnings growth. History has shown that competitive pressures are likely to change, and growth rates and valuations can compress. Very few companies can sustain a high level of growth and valuation over a long period of time. We have no doubt that many of today's anointed growth companies will still be around in 20 years, but we are willing to bet that their return profiles will not be as strong.

As illustrated in the following chart, leading up to the financial crisis of 2007-09, the price-to-earnings (P/E) premium for the MSCI EAFE Growth versus MSCI EAFE Value indices was largely range-bound between 20-40%. As we approached the market bottom in 2009, the valuation spread reached parity as growth multiples compressed while value multiples

started to recover. In the early innings of today's bear market, we could not be further from this reality. The growth premium has exploded in recent years and the spread has continued to widen, even as the market has retrenched. Today, the P/E premium for growth versus value is in excess of 98%.



Any semblance of reversion to the mean would result in much brighter days for value stocks. Investors have been trained to buy growth stocks, and eventually, that psychology will change. Investing based on fundamental value appears to have been lost in recent years, thanks in part to euphoria from experimental central bank policies (such as QE) and negative interest rates. While valuation doesn't seem to count for much today, we are confident that it will in the fullness of time.

Portfolio Activity

Given the massive dislocation in the market, we were active in the quarter and worked down our cash, a testament to the improved opportunity set. When fear became pervasive, great businesses started to trade at significant discounts to their intrinsic values. We added to our travel names, including Booking Holdings, Safran, and Whitbread, taking a long-term view that global travel will normalize over time. Each one has a solid, industry-leading balance sheet. We are confident that they will not only survive but will come out stronger on the other side. We also boosted our position in Compass Group, the largest food service company in the world, which has historically been a high-quality compounder with defensive characteristics. With empty stadiums, universities, and businesses, COVID-19 has had an acute impact on Compass's near-term fundamentals, but they too have the balance sheet to see it through. We increased our position in B&M European Value Retail, which was hit hard on COVID-19 and Brexit concerns (weak UK demand and China supply chain issues). The business sells essential products, so most of their stores will remain open during the UK lockdown. If the economy remains weak in the months to follow, B&M's discount retail concept should benefit. In addition to those discussed above, we also added to Sony, Philips, CK Hutchison, CNH Industrial, Bureau Veritas, and LG Household & Health Care, among others.

The increased volatility also provided the opportunity to upgrade the quality of the portfolio, exiting two of our lowest-conviction ideas, Nutrien and Electrolux, while adding three new investments where we found better long-term value: Lloyds Banking Group, Akzo Nobel, and Yokogawa Electric. In Lloyds, we were able to purchase a well-capitalized, low-cost, high-quality bank trading at around half of tangible book value. In Akzo Nobel, we bought one of the largest manufacturers of paints and coatings in the world, with strong brands and market-leading positions across consumer and industrial end-markets. We featured Akzo Nobel in our December 2018 letter, as part of our "Holiday Wish List" of companies we coveted. In Yokogawa Electric, we were able to invest in one of the world's premier process automation companies. With a fantastic balance sheet, Yokogawa is well-equipped to handle incremental weakness in

their oil & gas end-markets (under 30% of sales). After adjusting for cash and investments, the stock traded down to a high single digit earnings multiple.

At the end of the March quarter, the FMI International portfolios traded at a ~37% discount to the MSCI EAFE benchmark, using a selection of valuation metrics (see table below). Absolute values in the FMI International portfolio are more compelling today than they have been for quite some time, providing a very attractive setup for the years ahead.

March 31, 2020 Weighted Average Valuations*	FMI International	iShares MSCI EAFE	Discount to the Benchmark
P/E (1 Year Trailing)	14.9x	22.3x	33%
FY1 P/E (1 Year Forward)	13.4x	18.8x	29%
P/S	1.3x	2.9x	55%
EV/EBITDA	8.6x	12.6x	32%
Average Valuation Discount			37%

** Estimated valuations for FMI and the iShares are weighted average valuation calculations, not reweighted to exclude cash, and financial companies are excluded from the EV/EBITDA calculation. Valuations for both the portfolio and the ETF are modified based on criteria identified by FMI. For more detailed information regarding these valuations, please contact FMI.*

We appreciate your trust in FMI. Our philosophy and research process remain constant and our team is committed to delivering superior risk-adjusted results. Please see below for additional color on several investments where we are finding value.

Booking Holdings Inc. (BKNG) — Analyst: Benjamin Karek

Booking is the world's largest online travel agency. Booking's business model is asset light; they do not own any hotels. We believe the company still has a long growth runway, though temporarily derailed by COVID-19. Booking is primarily exposed to leisure travel, which we expect to be resilient over time. The business tends to take market share in downturns as hotel providers try to fill rooms through any channel possible. Booking is the best in the world at acquiring travelers at cheap prices, which inevitably means hotels will lean heavily on it through this downturn. We expect Booking to take share from competitors (e.g., Expedia) who may have to shrink their organization meaningfully just to survive. We estimate that >50% of Booking's costs are variable. With $2.7 billion in net cash and investments, we are confident that this stock will be a survivor and come out stronger on the other side. Given that, the low double-digit 2019 free cash flow multiple seems attractive.

Compass Group PLC (CPG LN) — Analyst: Dain Tofson

Compass is the largest food service company in the world. It's a high-quality business with a track record of success. They differentiate in three main ways: (1) a focus on food service, not ancillary services (i.e., facility management or janitorial services); (2) leveraging the group's large purchasing organization (Foodbuy); and (3) going to market with multiple brands, which is beneficial for demand segmentation. Although Compass has historically been rather defensive in economic downturns, the COVID-19 pandemic and subsequent global shutdown has significantly impacted the group with run-rate revenue down around 50%. We believe that Compass can navigate this challenging environment and come out even more advantaged, as the reaction to the COVID-19 situation will likely wipe out weaker competitors. The balance sheet is strong at roughly 1.5 times net debt-to-EBITDA,[1] and they have substantial liquidity with a £2 billion revolver and significant headroom against their covenants. The stock declined over 30% year-to-date and now trades at a low-teens earnings multiple. Compass has generally traded in the high-teens/low-twenties. If they can get back to the fiscal year 2019 earnings in a few years, this should be a very good investment from here.

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[1] Earnings before interest, taxes, depreciation, and amortization.

CK Hutchison Holdings Ltd. (1 HK) — Analyst: Andy Ramer

This blue-chip company owns relatively defensive, high-quality businesses that generate recurring and sustainable earnings. Telecom (higher voice and data usage) and Infrastructure (electric & water distribution and transportation), which together account for 60% of EBITDA, should be relatively immune to the current events. CK Hutchison has a strong balance sheet to weather the downturn. This is reflected in its investment grade credit rating of A/stable. The net debt-to-capitalization ratio is 25%, with a debt maturity profile that is long and balanced. The conglomerate generates a prodigious amount of free cash flow, which the market is currently valuing at a 15% yield. The stock is trading at a greater than 60% discount to its net asset value, and insiders have recently been buying. This represents more than a two standard deviation discount to the historical mean.

Ferguson PLC (FERG LN) — Analyst: Jordan Teschendorf

Ferguson is the world's largest distributor of plumbing and heating products to trade professionals, with nearly all their business in North America. The company's scale, branch density, and distribution footprint provide it with a competitive advantage in terms of purchasing, fulfillment, contractor relationships and superior service levels compared to its fragmented competition. Over the last decade, Ferguson has focused on organic growth and returns, strengthening its already market-leading U.S. business and divesting operations in several less attractive geographies. Today, approximately 60% of Ferguson's sales are driven by remodeling, maintenance and improvement work (versus 31% in 2008). This type of business is less cyclical and typically carries higher margins than sales to the new build market. Ferguson has a terrific long-term track record, with operating profit growing at a double-digit compounded annual growth rate over the trailing 10, 20, and 30-year periods, respectively. We believe the customer value proposition continues to strengthen with scale and flows to improving economics for shareowners (return on capital employed has more than doubled from a decade ago). While end markets served are clearly cyclical and the outlook uncertain, the business is operating from a position of strength with conservative net leverage, strong liquidity, an experienced management team, and an inherently variable cost structure (>60% of operating expense is labor). The stock is valued well below long-term averages.

Samsung Electronics Co. Ltd. Pfd. (005935 KS) — Analyst: Daniel Sievers

Samsung has the world's dominant semiconductor memory business (#1 in DRAM & NAND technologies). The DRAM market once had dozens of gasping players, but is today dominated by three (Samsung, SK Hynix, and Micron). In terms of technology and cost, this market has become very difficult to enter, helping to reduce high cyclicality. The NAND market has an additional 2-3 significant players, but the trend has been toward similar consolidation over time. Samsung makes more money at every point in the cycle than DRAM/NAND peers and has outsized influence over the industry. Samsung is also a leader in Semiconductor Foundry, Display Technology; is #1 in the World for Smartphone production; makes tablets, PCs, and medical devices; and is a leading global manufacturer of home appliances. We own Samsung's preferred shares. They pay a 3.4% dividend yield and trade at a discount to the common stock. Samsung has a whopping $80 billion (USD) in net cash on the balance sheet, so at a high single digit P/E multiple, we like the long-term outlook.

Thank you for your confidence in Fiduciary Management, Inc.

Fiduciary Management Inc.
International Equity Composite
12/31/2010 - 12/31/2019

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation		Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
						Composite	*Benchmark			
2011	-0.78	-1.52	-12.15	1	0.00	n/a	n/a	$ 16.7	$ 12,273.6	0.14%
2012	19.35	18.46	17.31	1	0.00	n/a	n/a	$ 76.3	$ 15,253.5	0.50%
2013	25.89	24.95	26.93	1	0.00	9.78	12.22	$ 165.8	$ 19,705.3	0.84%
2014	5.66	4.87	5.92	1	0.00	7.49	10.33	$ 771.6	$ 21,001.1	3.67%
2015	4.24	3.46	5.33	2	0.00	8.14	11.73	$ 2,832.9	$ 21,042.9	13.46%
2016	11.04	10.23	5.34	3	0.38	7.39	11.53	$ 5,946.2	$ 22,626.7	26.28%
2017	16.51	15.70	15.23	3	0.02	7.04	11.20	$ 8,209.3	$ 25,322.0	32.42%
2018	-8.63	-9.27	-10.99	3	0.06	7.22	9.69	$ 6,287.8	$ 19,833.6	31.70%
2019	18.11	17.29	21.67	3	0.08	8.30	9.48	$ 7,522.0	$ 22,609.8	33.27%

*MSCI EAFE Net Local Index®

Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Incorporated (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 12/31/2019. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The International Equity Composite has been examined for the periods 12/31/2010-12/31/2019. The verification and performance examination reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $22.6 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The International Equity Composite was created on December 31, 2010. This composite invests mainly in a limited number (usually between 25-40) of large capitalization (namely, companies with more than $5 billion market capitalization) foreign companies.

The International Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes. Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2011, the trailing three year annualized ex-post standard deviation for the Composite and Benchmark are required to be stated per GIPS®. For the periods 2011-2012, the information is not available for the International Equity Composite.

Currently, the advisory fee structure for the International Equity Composite portfolios is as follows:

Up to $25,000,000	0.70%
$25,000,001-$50,000,000	0.65%
$50,000,001-$100,000,000	0.60%
$100,000,001 and above	0.55%

The firm generally requires a minimum of $25 million in assets to establish a discretionary account. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The MSCI EAFE Net Local Index® is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Net Local Index consists of the following 21 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. It is reported in local currency and net of hedges. The International Equity composite uses the MSCI EAFE Net Local Index® as its primary index comparison.

Fiduciary Management Inc.
International Equity Unhedged Composite
12/31/2019 - 03/31/2020

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation Composite	Three Year Ex-Post Standard Deviation *Benchmark	Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
Q1 2020	-29.09	-29.22	-20.55	1	0.00	n/a	n/a	$ 26.5	$ 15,121.8	0.17%

*MSCI EAFE Net Index (USD)®

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FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $22.6 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The International Equity Unhedged Composite was created on December 31, 2019. This composite invests mainly in a limited number (usually between 25-40) of large capitalization (namely, companies with more than $5 billion market capitalization) foreign companies.

The International Equity Unhedged Composite reflects time-weighted and asset-weighted returns for all discretionary accounts. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes. Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2019, 36 months of performance is not available; therefore the three year annualized ex-post standard deviation is not presented for the composite or the benchmark.

Currently, the advisory fee structure for the International Equity Unhedged Composite portfolios is as follows:

Up to $25,000,000	0.70%
$25,000,001-$50,000,000	0.65%
$50,000,001-$100,000,000	0.60%
$100,000,001 and above	0.55%

The firm generally requires a minimum of $25 million in assets to establish a discretionary account. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

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