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THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Targeting U.S. Large Caps With Consistent Cash Flow Growth

SEAN CHAITMAN is the President and Chief Investment Officer of Shelter Rock Management. He has three decades of investment experience as a portfolio manager and a research analyst. Prior to Shelter Rock, he was a member of the investment team at Heirloom Capital Management, a long and short equity fund. Mr. Chaitman was also previously a senior equity research analyst at Jesup & Lamont Securities Corporation and a member of Smith Barney's value stock research team. He has an MBA from Columbia Business School and a B.S. in Economics from the University of Wisconsin at Madison. He has been quoted and featured in *The Wall Street Journal, Investor's Business Daily, Forbes* and *The Wall Street Transcript*.

SECTOR — GENERAL INVESTING

TWST: It has been a few years since you last spoke with us, so let's start with a refresher on Shelter Rock Management, a bit about the company's history and your business today.

Mr. Chaitman: We're an independent, SEC-registered investment adviser. We're based in Jericho, New York, and our company was founded in 2006. We have an experienced team of investment professionals in portfolio management, research, trading and advisory who all work hard to provide a positive experience for our clients.

Our growth and income strategies are suitable for high-net-worth investors, family offices, charitable organizations and other RIA firms as a subadviser. Our strategies are included in institutional databases, such as Morningstar, PSN-Informa and eVestment, that profile peer managers.

We're proud that three of the four strategies we manage were awarded Morningstar's highest five-star overall rating for the first and second quarter of this year. These ratings were based on our strategies' risk-adjusted returns over the three-, five- and 10-year periods.

TWST: Is there anything else you would add in terms of what you feel differentiates Shelter Rock from peers or competitors?

Mr. Chaitman: Being an independent firm has many advantages. We leverage the resources of large companies like Fidelity and we have the flexibility to invest in what we consider to be the best investment opportunities for our clients.

We've developed our own investment processes that we have been following since the firm was founded close to 20 years ago. We have professionals who have invested across many different market cycles, using both growth and value processes and through different types of bull and bear markets. Our processes have produced strong long-term returns for our clients and we expect this to continue.

Finally, the level of personalized and attentive client service that we provide differentiates our company. Our clients always come first, and we value each client relationship. We understand our clients' personal profiles and we develop investment plans to help them achieve their long-term goals.

TWST: You have three strategies that contain equities. Do you want to give a quick snapshot of these strategies before we get into more specifics about large cap stocks?

Mr. Chaitman: Our strategies contain similar stocks that we weight differently to address our clients' risk profiles. This approach allows us to focus our research efforts on our best ideas. It also enables an easy transition from an investment and a tax standpoint when our clients enter into retirement and need a more conservative strategy.

Our Select Equity strategy is an all-equity portfolio that has up to 25 of our highest conviction U.S. large-cap stock selections. Next, we have our Equity Income strategy, a balanced portfolio for moderate risk profiles, which has up to 75% of its portfolio in stocks and the rest is in bonds. And finally, we have our Conservative Allocation strategy, our most conservative equity strategy. It has up to 40% of its portfolio in stocks and the rest in bonds.

TWST: In terms of the equity portion of those strategies, it's really focused on U.S. large-cap stocks. Could you talk a bit about why just large caps? What's the investment philosophy or reasoning behind that?

Mr. Chaitman: We invest with the goal of producing consistently attractive long-term returns for our clients over every market cycle. In baseball terms, we like to describe our approach as batting for singles and doubles to consistently advance the runner, as opposed to swinging for home runs where you can run the risk of striking out.

This leads us to invest in high-quality and attractively valued U.S. large-cap stocks that are experiencing long-term secular growth trends, and in businesses that are recession-resistant. Importantly, the companies we look to invest in have a history of continuously growing their cash flow.

Smaller-cap stocks tend to be more volatile, and they can be highly susceptible to macroeconomic shocks and market liquidity risks. International stocks have currency translation and political risks that add an additional layer of uncertainty and unpredictability.

Since we try to minimize external risk to the greatest extent possible, we are mostly focused on investing in U.S. large-cap stocks.

TWST: Walk us through your research and investment process. And what would you add about other characteristics you're looking for in holdings?

Mr. Chaitman: As I mentioned, our processes are focused on investing in companies that have a history of continuously growing their cash flow. Not a lot of companies fall into this category, so it's a fairly select universe of high-performing businesses.

a company's free cash flow yield. This is our preferred valuation metric. When a stock screens well on all of these metrics, we will consider it for our strategies.

TWST: Can you share with us a few examples of holdings? They could be in your top 10, or notable or interesting for other reasons.

Mr. Chaitman: Booking Holdings (NASDAQ:BKNG) is a new position that we added earlier this year after the shares sold off from some of the tariff concerns. The company is the leading online travel agency through its Booking.com, Priceline, KAYAK, and OpenTable brands.

Consumers are increasingly booking their vacations online, and we expect this trend to continue. The company has a large competitive advantage with a network of 30 million accommodation listings. This drives traffic to its site and creates a halo effect for its other travel services.

Financially, the company has grown its free cash flow at a double-digit annualized rate over the last decade. We think the shares are attractively valued at a 6% free cash flow yield.

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We follow what I would describe as a top-down, bottom-up equity investment process. Most of the stocks we invest in are market leaders in large and growing industries. They tend to have large barriers to entry that protect what are often high-profit-margin businesses.

1-Year Daily Chart of Booking Holdings Inc.

Chart provided by www.BigCharts.com

We also look to invest in companies that have a track record of maximizing shareholder value, whether it's through organic growth, accretive acquisitions, large share repurchase programs, dividends, or even a combination of each.

On a company-specific research level, we analyze business and industry trends, and create financial models that help us determine

Another long-term secular trend that we're invested in is artificial intelligence. We're invested in a few industrial businesses that are benefiting from the massive investment to build-out AI infrastructure. One of our top holdings, **Trane Technologies** (NYSE:TT), is a leading provider of commercial HVAC systems that are being used in data centers that support artificial intelligence applications.

TWST: AI has obviously been a big theme in recent months and the last few years. Are there particular sectors that you are intentionally overweighting or underweighting these days?

Mr. Chaitman: We typically do not invest in traditional money center banks, investment banks or regional banks. These businesses are highly regulated and cyclical. They don't have consistent cash flow. Banks also have opaque balance sheets and we've seen how this has played out at times. I think we all remember what happened to Lehman Brothers, Bear Stearns, Washington Mutual. More recently, we saw what happened to Silicon Valley Bank.

We also do not own energy stocks. These businesses tend to be commodity driven and their fundamentals are usually tied to the underlying commodity.

I would also point out that many of the types of stocks that we invest in are not immune from market volatility, but as long as we have line of sight that they'll continue growing their cash flow, we can get a high confidence level and conviction that the share prices will continue to appreciate.

They also tend to rebound fairly sharply after we go through volatile periods, and a reason for that is, investors tend to gravitate to the

safety and strength of U.S. large-cap stocks that have durable and growing cash flow streams.

TWST: What were your biggest contributors and biggest detractors in the last quarter or two? Do you think they were company-specific situations, or does it point to trends within certain sectors or industries?

Mr. Chaitman: Nvidia (NASDAQ:NVDA) is a top holding in our strategies and the shares have continued to perform well. The company is experiencing strong demand for its AI semiconductors from its hyperscaler and government customers who are racing to adopt this technology.

Another company that's performed well this year is **O'Reilly Automotive** (NASDAQ:ORLY). The company recently raised their comparable store sales guidance. The business is countercyclical and benefits from economic uncertainty. Americans are driving their cars for longer, and they're putting more wear and tear on them. This has been creating more store traffic since most of their products are essential car parts, like wipers and brakes.

Accenture's (NYSE:ACN) shares have been a detractor this year. The company has been affected by the soft global economy as their large enterprise customers have been deferring their IT spending.

TWST: Historically, how have U.S. large caps tended to perform in different market and economic environments?

Mr. Chaitman: At a high level, I think we can say that U.S. large caps tend to outperform during the earlier stages of an economic cycle, and also during difficult market environments.

As we talked about, we're a little bit more situational specific, and I'll give you one more example of a stock that exemplifies what we look for with our strategies. The company is **TJ Maxx** (NYSE:TJX), which we've owned for a lot of our clients for the better part of the last decade.

When times are good, you can buy a polo or some underwear or socks at a TJ Maxx or Marshalls and pay half the price of a department store. And when the economy is bad, you can also buy the same items for a fraction of what it costs elsewhere.

Since they buy large quantities of their inventory from department stores that are looking to clear out items, they can get great deals on high-quality brands and make a nice profit on them.

TWST: How would you describe where we are today as it relates to the economy?

Mr. Chaitman: We've been through an unusual time. The economy has experienced hyperinflation for the first time since the 1970s. The rate of inflation has stabilized recently, but prices are still much higher compared to where they were a few years ago.

Interest rates have been stubbornly high, and that's been weighing on the consumer. Housing has been unaffordable for a large part of the population, and it's expensive to run a balance on a credit card or buy a new car.

With that said, there is a silver lining. We may be at the beginning of a turning point. The Fed is now talking about potentially easing its monetary policy, which could be positive for stocks as we move into the second half of this year.

We're also mindful that anything can happen at any time in the markets, and we always try to remind ourselves and our clients why it's important to focus on the long term. Of course, that can be easier said than done, as we know.

TWST: What are the biggest risks you see, for your client portfolios but also the market more broadly?

Mr. Chaitman: One of the biggest risks that we're monitoring is the potential for stagflation, where we go into a period of higher inflation and slower economic growth.

If this were to occur, we would expect our approach to fare well since we invest in companies experiencing secular growth trends that are positioned to outperform regardless of the state of the economy.

TWST: Thank you.

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