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TRANSCRIPT
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Quality Mid Cap Fund Quarterly Update: 4Q 2024

Hosted by Kurt Havnaer, CFA, Portfolio Manager

KURT HAVNAER: My name is Kurt Havnaer. I'm one of the portfolio managers on the Jensen Quality Mid Cap Fund. I'd like to welcome you to our fourth quarter webinar. Here is our agenda for today's webinar. We will begin by reviewing the fund's performance and some of the changes that we made to the portfolio during the fourth quarter. We will then provide our outlook for 2025 and then open the webinar up for Q&A. Before jumping into performance, we would like to provide a brief overview of Jensen and our philosophy for the Mid Cap Strategy. Jensen was founded in 1988. Our firm is owned by approximately half of our current employees. We manage $11.2 billion in assets in three primary investment strategies: Jensen Quality Growth, Jensen Quality Mid Cap and Jensen Global Quality Growth.

In terms of our philosophy for the Mid Cap Strategy, we believe that undervalued stocks of high-quality companies represent attractive investment opportunities. We define a high-quality company as one with strong competitive advantages. If a company has strong competitive advantages, that should enable it to generate high returns on capital, and if the company's return on capital exceeds its cost of capital, that is what drives the value of the business higher in the future.

Moving on to performance, slide 5 shows the fund's net returns over various time periods through December 31st, 2024. As you can see, the fund underperformed its primary benchmark, the Russell Midcap Index, during the fourth quarter, and over the past one- and three-year periods. With an annualized return of 10.1%, the fund outperformed its benchmark over the past five years.

The next slide compares the fund's gross returns for the fourth quarter to the Russell Midcap Index. As shown in the last row of the table on the

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left, the fund's gross return of minus 4.21% was lower than the Midcap Index, which was up 0.62%. During the quarter and for all of 2024 for that matter, the Russell Midcap Index return was dominated by a small number of very large market cap companies whose stocks increased sharply. For example, Palantir Technologies, the largest market cap company in the index, accounted for more than 100 basis points of the value of the index and its stock was up 103% during the fourth quarter. Similarly, AppLovin Corp, the second-largest market cap company in the index, saw its stock increase 148% during the fourth quarter. Both of these companies are benefiting from the AI boom and neither is included in our investable stock universe. From a sector standpoint, the fund's underweights in Financials and Energy stocks and overweight in Health Care stocks were the largest sector detractors from relative performance.

Our underweights in Real Estate and Utilities stocks were the two largest sector contributors to relative performance. On the right-hand side of the slide, you can see the top five individual contributors to and detractors from relative performance. We can discuss any of these 10 names during the Q&A, but we would like to provide some commentary on both Copart and Booz Allen Hamilton on the next two slides.

As indicated on the previous slide, Copart was the largest individual stock contributor to performance during the quarter. Copart owns automobile wrecking yards and conducts online auctions for damaged vehicles supplied primarily by auto insurance companies. We believe the stock outperformed during the quarter due to the company reporting strong sales and earnings growth during its most recent quarter and to a decline in used car prices, which is generally positive for auction volumes. Copart remains a core holding in the portfolio due to the company's strong market share, significant barriers to entry, solid economies of scale and strong balance sheet with no debt. We also believe the company's stock is attractively priced.

Booz Allen Hamilton was the fund's largest individual stock detractor from performance during the quarter. Booz Allen is a management and IT consulting firm with approximately 97% of its revenues derived from contracts with agencies of the U.S. federal government. We believe the stock underperformed due to the new administration's pledge to reduce government spending and the market's belief that this could negatively impact the company's revenue growth. We actually believe the opposite. In our minds, Booz Allen will benefit from the government's efficiency efforts as many of the company's contracts are mission-critical and they streamline government functions. Long term, we like the company's contracted revenue streams, which represent a barrier to entry, its high recurring revenues, and strong new contract win rate. We also believe Booz Allen stock is attractively priced.

Moving on to portfolio changes. During the quarter, we purchased Hologic and Ross Stores and liquidated several names. Hologic develops, manufactures and sells diagnostic instruments, medical imaging systems and surgical products focusing primarily on women's health. We added the company to the portfolio due to its well-known brand in served markets, its large installed base of Panther diagnostic instruments, its high recurring revenue streams and switching costs, and the attractive valuation on the company's stock. Ross is the second-largest off-price retailer of apparel and home furnishings, selling products at discounts ranging from 20% to 60% versus traditional retailers.

Long term, we like the company's solid market share, the countercyclical nature of its business and its economies of scale versus peers such as Burlington and Nordstrom Rack. We also believe Ross's stock is attractively priced. In terms of sales, Pool, United Rentals and Waters Corporation were sold primarily for valuation reasons. Our investment process incorporates disciplined sell triggers that are based on a combination of company fundamentals and the valuations we get from our valuation models. All three of these stocks tripped our sell triggers during the quarter and were sold as a result. We like the long-term fundamentals of all three of these companies and we'd be happy to add them back to the portfolio at the right price.

Charles River Laboratories is a supplier of products and provider of services primarily to biotech and pharmaceutical companies. We sold the position due to concerns about drug discovery spending by the company's biotech and pharmaceutical customers. ULTA Beauty is a specialty retailer of cosmetics, fragrances, and skin and hair care products. We liquidated the position during the quarter due to increased competition and share losses

stemming primarily from expansion by Sephora, one of the company's primary competitors.

Moving on to our outlook for the economy and markets. Not surprisingly, a number of tailwinds exists that support that outlook and a number of headwinds exists that could pressure economic growth and market performance going forward. In terms of tailwinds, the next two slides indicate that the U.S. labor market remains strong. This strength could lead to solid consumer spending, which as a reminder, accounts for approximately two-thirds of GDP in the U.S. This graph shows the year-over-year change in monthly average hourly earnings going back to 2007. While hourly earnings growth declined over the past couple of years, it remains above the historical average of 3.1%.

The graph on slide 12 shows the U.S. unemployment rate going back to the late 1940s. At 4.2%, the current unemployment rate remains well below the historical average of 5.7%. The decline in the rate of inflation over the past couple of years is arguably another tailwind for the economy in markets. This graph shows the year-over-year change in monthly core personal consumption expenditures, the Fed's preferred measure of inflation, and the data goes back to 2003. While still above the long-term historical average of 2.1%, the inflation rate declined significantly from its recent peak of 5.6%. Another tailwind is the expected improvement in corporate earnings. Slide 14 shows that earnings growth for companies in the S&P 500 is expected to increase in 2024 and 2025 following weakness in both 2022 and 2023.

In terms of headwinds, the strong market rally that began during the fourth quarter of 2023 appears to have pushed equity valuations to relatively expensive levels. This graph shows the monthly forward P/E on the S&P 500 going back to 1999. At the end of 2024, the forward P/E of 21.7 times the S&P 500 exceeded its historical average of 16.6 times and was more than one standard deviation above that long-term historical average. Despite the previously mentioned strengthened wages and employment and the recent decline in inflation, consumers do not appear to be very optimistic about the U.S. economy. This graph shows the University of Michigan's Consumer Sentiment Index going back to 1978. The index measures consumer attitudes and expectations about the economy. While the index improved from its recent low, it remains below the historical average suggesting that consumer spending could be sluggish going forward.

The next slide is a measure of consumers' financial health. It shows the ratio of household debt service payments to disposable income going back to 1980. As you can see, the ratio declined significantly from its peak of 15.8% during the financial crisis. While the ratio remains below the long-term historical average of 11.9%, it increased sharply since 2021 suggesting that consumers' financial health may be deteriorating. The next slide tells a similar story. This graph shows that the delinquency rate on consumer loans, while still below the long-term historical average of 3.1%, has increased meaningfully since 2021. This suggests again, that consumers' financial health may be weakening.

Slide 19 shows that financial distress might also be increasing for corporations. Specifically, this graph shows the absolute number of corporate bankruptcies in the U.S. on an annual basis going back to the tail end of the financial crisis back in 2010. Corporate bankruptcies have rebounded from low levels in 2021 and 2022, and we're at a 14-year high in 2024. The next two slides show what happened to interest rates before and after the first reduction in the Fed funds target in the current rate-cutting cycle. Specifically, slide 20 shows that the yield on 2-year Treasury notes declined heading into the first reduction in the Fed funds rate back in September of last year. This decline is consistent with historical patterns indicating that bond investors anticipated the first rate cut. What's different this time around is that the yield on 2-year Treasury notes increased after the first rate cut. Historically, yields on longer-dated treasury notes tend to continue to decline after the initial reduction in the Fed funds rate.

The graph on slide 21 shows that the yield on the 10-year Treasury note followed a similar path to the yield on the 2-year shown on the previous slide. The decline in the 10-year yield before the initial reduction in the Fed funds target is consistent with historical patterns, but the subsequent increase is not. These unusual movements in long rates, following the initial reduction in the Fed funds target, could be the bond market signaling that it expects inflation to rebound. Such an increase would most likely be negative for both consumers and corporations. Finally, the next slide shows GDP growth over the past five years and

forecasts from 2024 through 2027. As you can see, GDP growth is expected to decline in 2024 from the levels seen in 2023. GDP growth is also expected to remain below the long-term historical average of 2.7% in each of the next four years.

To conclude, as we've discussed in previous webinars, we believe it is very difficult to predict the short-term direction of the economy and equity markets. Numerous factors could strengthen the economy and continue to drive the market higher. Others could weaken the economy and cause the market to drift sideways or trade down. Despite these uncertainties, we will continue our strategy of investing for the long term and purchasing undervalued stocks of high-quality companies with strong competitive advantages and high returns on capital. We believe this strategy should result in attractive risk-adjusted returns throughout various economic and market cycles. And with that, we can now open the webinar up for Q&A.

The Jensen Quality Mid Cap Fund's investment objective, risks, charges and expenses must be considered carefully before investing. The statutory and summary prospectus for each fund contain this and other important information about the investment company, and they may be obtained by visiting www.jenseninvestment.com or by calling 800.992.4144. Read it carefully before investing.

Mutual fund investing involves risk, and principal loss is possible. The Fund invests in mid- and smaller-capitalization companies, which involve additional risks such as limited liquidity and greater volatility. Value stocks have a lower expected growth rate in earnings and sales than growth stocks.

Visit www.jenseninvestment.com for the Jensen Quality Mid Cap Fund's current performance, including the 5 year upside/downside capture. Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Fund may be lower or higher than the performance quoted. All returns include the reinvestment of dividends and capital gains. To obtain updated performance information that is current as of the most recent month end, please call 1-800-992-4144 or visit www.jenseninvestment.com.

On September 30, 2024, the Jensen Quality Value Fund was renamed the Jensen Quality Mid Cap Fund.

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