White Brook Capital
860 Sheridan Road
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First Quarter 2024 Commentary

Quarter in review

Performance Review

As of March 31st, 2024

NAV increase, net	Cum Incept	PF 2019	2020	2021	2022	2023	1Q/24
WBCP	82.04%	17.60%	19.05%	37.16%	(15.38%)	8.38%	3.36%
S&P 400	66.88%	5.72%	13.66%	24.76%	(13.06%)	16.45%	9.96%

Inception of White Brook Capital Partners was August 16, 2019
Performance figures are provided by the administrator. Prior years are audited. 2024 is unaudited
Performance is net of all realized and accrued fees

Market Review

Eid Mubarak to those who celebrate.

During the first quarter, markets were risk-on, with the performance of the S&P 500 surpassing even the most optimistic projections. In my view, the S&P 500 continues to be expensive on a historical and relative basis, while mid-cap and small-cap stocks are cheap both relatively and absolutely. A reassessment of expectation regarding Federal Reserve determined interest rate deductions from 6-7 at the beginning of the year to 0-2, now, due to varied but persistent inflation trends is again dramatically slowing transactions in large and income generating asset transactions as buyers incorporate higher financing costs than expected and sellers are unwilling to lower their asking price for a potentially temporary environment.

During the first quarter, the artificial intelligence theme maintained its positive momentum, buoying the S&P 500 and Nasdaq, extending the trend observed in the previous year. However, shifting interest rate expectations and the release of competitive AI chips by major customers in April have introduced a degree of uncertainty regarding the potential profitability of this investment theme. Consequently, the S&P 500's momentum has begun to diminish.

In early April, the disparity between subprime and affluent consumers and their spending patterns continued the divergence observed throughout 2023, with inflation further compromising the financial well-being of lower-income consumers while affluent consumers maintain healthy spending levels. During the quarter, the portfolio was repositioned to more acutely exploit those dynamics.

Portfolio Review

White Brook Capital Partners made three new investments during the quarter, Lifetime Holdings Group, Inc (LTH), PetIQ, Inc (PETQ), and Portillo’s, Inc (PTLO). Each of which I believe will be long term holdings, are grossly undervalued, and will build value at an accelerated pace both in the short and long term.

The biggest gainers during the quarter were Builders First Source, Inc (BLDR), The Greenbrier Companies, Inc (GBX), and Openlane. Inc (KAR). The biggest losers in the quarter were B. Riley Financial, Inc (RILY), Afya Limited (AFYA), and Green Plains, Inc (GPRE).

During the quarter, we sold Knight Swift Transportation (KNX) and B. Riley Financial (RILY). Riley has outperformed since our sale. I continue to believe the short thesis to be incorrect, and based on asset value alone, for there to be significant upside to the stock. But companies aren't just assets, and the Company's inability to file its financial statements on time because it focused on clearing itself of a few of the accusations made by short sellers reflected management and the board's misplaced focus. The short strategy of flooding the zone with misinformation worked and is detracting from the source of its competitive advantage - management's attention.

After underperforming during January and February, the disposal of two investments and the addition of three new positions coincided with much improved performance in March.

Investment Focus: PETIQ (PETQ)

PET IQ
Smarter Pet Health

Overview

Consensus	2023	2024	2025
EV/Sales	0.7x	0.7x	0.6x
EV/GP	3.1x	2.9x	2.7x
EV/EBITDA	7.5x	7.1x	6.4x
P/E	12.7x	12.5x	10.8x
FCF Yield	7.8%	8.9%	8.9%

PetIQ, Inc. is a United States based generic pet medication, supplements, and wellness services company. The Company operates as a value-added intermediary between club, big box retail, and ecommerce companies; pet pharmaceutical companies; and the consumer.

PetIQ consists of two reportable business segments: product and services. The product segment, which constituted their original business, is a distribution operation that distributes over-the-counter and prescription pet pharmaceuticals to retailers. Subsequently, the organization has expanded to include a proprietary products business that manufactures PetIQ-branded generic and over-the-counter pharmaceuticals and supplements for distribution to pharmacies and retail stores. The services segment offers veterinary services at retail establishments. This segment is instrumental in stimulating consumer demand for high-profit, per-square-foot pet items and generates rental income for associated retailers. Notably, 50% of their customers have never visited a veterinarian prior to seeking services from a PetIQ facility.

Underlying industry trend: Pet adoption increased significantly during Covid. After society reopened, the rest of the pet industry has suffered from a lull in pet spend and slowing growth in categories associated with the purchase of a new pet. Pet destruction has not increased, however. I believe, as pets age, medications and supplements and Primary care-like vet services, PetIQ's businesses, will continue to prosper.

Over the past couple quarters, two more acute dynamics are occurring. More affluent customers continue to humanize their pets and spend on premium goods and services. Less than affluent customers are more acutely feeling the effect of inflation and are still spending on their pets, but are trading down. This dynamic favors PetIQs more cost effective products and services.

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Near/Medium Term PT: $45+ (Curr Price, $17.50). While many companies in the pet sector over-earned during Covid lockdowns, PETIQ benefits from a pet's continued existence - not just the initial purchase. The Company's growth algorithm is for 10% revenue growth, and 15% EBITDA growth. Whether valued as a distributor or as a branded merchandiser, the products division should be rerated higher. The services business has under-earned since Covid, but that should end in the near term, resulting in improving ROIC and a better deserved valuation.

The products division has two different operations its own products business and its distribution business:

1) 30% of product revenue is generated from branded products the company manufactures.

This business resembles a typical consumer packaged goods business. Two major drivers of the company reside within this segment; the Supplements business and the Flea and Tick medication business.

In 2Q23, supplements became the Company's largest single business. Its brands include Minties and Rocco and Roxie, and PetIQ is a private label manufacturer for Costco's Kirkland brands. It continues to launch products in the space and grow in the premium and mainstream categories. The total addressable market in supplements is large and growing. White Brook models this business as a 15% long term grower, higher in the short and medium term, with CPG EBIT margins.

The Company also manufactures tick and flea medication. This business is essentially a toll booth on the weather in the United States with more temperate winters and springs resulting in higher tick and flea pet infections. Climate change is, unfortunately, a positive for PetIQ as vets report that tick and flea season is rapidly becoming a year round issue in more places. PetIQ has been growing market share, and currently sells a product in a little over ~18% of cases due to their products' efficacy, price, and distribution. This is a seasonal business and White Brook assumes that no tick and flea case goes unaddressed currently, so growth is limited to pet population growth, market share gains, and climate/weather change.

2) The bulk of the company's product revenue is earned from distributing prescription and OTC medications for other pet pharmaceutical companies into retailers and into their services business.

This is a decent distribution margin business where the company takes little risk. The inventory is relatively long-lived and can be moved easily as required with little risk of obsolescence and their distribution network is top-class, delivering product anywhere within 24 hours. The business should grow with pet ownership and care spend and enhanced by the services divisions' market share gains.

In 2023, the Company's own products grew ~28% and consolidated products segment grew ~20%. The Company guided that their own products should grow low double digits in 2024, implying that overall products should grow high single digits. I think this is likely a conservative estimate. Regardless, the growth in this business is from the higher margin owned products businesses which are also smaller businesses. As the business gets bigger, we should see faster segment growth, with higher margins all else being equal.

The Services division is a demand generator for retailers. It has two different service types and is becoming more capital efficient.

1. **Operates veterinarian services through community clinics.** A growing piece of the business, called community clinics, are vans that are set up within or just outside a retail store for 2-3 hours, for walk up appointments. The van travels to 3 locations a day, sometimes with a contracted vet on site, and is responsive to the demand at a particular location, scaling hours and visits per week as required.

   Contracted vets, when needed, bid on routes. On average they're paid ~$2,250 per day, when needed, this is up from $1,500 per day a few years ago.

   The economics of the community clinic are attractive. Clinics typically see 7-8 pets per hour, at an average spend of $100 a visit. Vets are paid approximately $2,250 per day, when needed, with a couple technicians aiding the vet. White Brook estimates that EBITDA margins for the business are around 30%.

2. **Wellness centers are permanent and more sophisticated veterinarian concepts in retail stores.** They can provide more sophisticated services, including diagnostic tests, vaccinations, prescription medications, microchipping, grooming and hygiene, and wellness checks; and other veterinary care services. During 2023, PetIQ closed about 45% of its Wellness Centers and expanded its community clinic program due to the shortage and increased costs of employing veterinarians. The last of the closure (wellness centers) and expansion costs (community clinics) should occur in 1Q 2024.

   To enhance the return profile of Wellness Centers the company is trialing a hygiene upgrade at its Wellness Centers. The upgrade requires $300k to enable, but the center then transitions to providing a more complete set of hygiene and grooming services that pet owners can pay an all you can eat $80/month subscription for access. With the elimination or more limited needs for vets within Wellness Centers that adopt the model, the returns could be significant if successful.

Acquisitions:

The Company has been a solid acquirer, initially acquiring large business to expand capability, but more recently finding tuck-in acquisitions that PetIQ can plug into its business.

1. 2023 Rocco & Roxy added premium brand and stain and odor category. Paid 9x forward EBITDA - after actualized revenue and cost synergies acquired at 4-5x EBITDA
2. 2020 Capstar (Tick & Flea) expanded Tick and Flea treatment compounds
3. 2019 Perrigo - Competitive brands and manufacturing facility
4. 2013 VIP Petcare - Last nationwide vet clinic not owned by Mars. Health centers and community clinic capability

BENCH Analysis - BEST, EASIEST, NECESSARY, CHEAP AND HEART (INCENTIVES)

ENC: Product is **e**asier to access, **n**ecessary, and **c**heaper than the alternative. Distributed products are **c**heaper than alternative distribution channels. Manufactured products are also **c**heaper than reference competitors.

ENC: Service is **e**asier to access, **n**ecessary, and **c**heaper than alternative channels for similar services. There are competitive services, although those operate in standalone, pet specific environments, and not bundled with general merchandise as they are through their retail partners. Service is **c**heaper than if a vet office completed them.

H: The Company is founder-run and the founder is dissatisfied with the Company's stock price. Compensation plans are not set to induce high returns on capital - focused instead on revenue and EBITDA growth, but the culture of the company and management is focused on each effort's contribution to return on capital.

White Brook agrees with the Company's focus on growth given the opportunity set ahead, but would like to see focus on investment returns institutionalized in the incentive structure. Overall, pay is high and more in line for a company of $1.5bn-$3bn in market cap in my view.

Comparables:

					2023		
Company	**EV/GP**	**EV/EBITDA**	**P/E**	**FCF Yield**	**Sales y/y gr**	**GP margin**	**EBITDA margin**
CAG US	6.3 x	9.4 x	10.5 x	8.9%	6.4%	26.6%	20.5%
LW US	9.0 x	10.9 x	17.2 x	3.0%	30.5%	26.8%	21.0%
POST US	5.8 x	9.9 x	21.0 x	5.1%	19.5%	26.9%	17.6%
NOMD US	5.3 x	8.6 x	10.3 x	7.1%	3.6%	28.2%	17.6%
LANC US	11.8 x	18.2 x	30.2 x	2.6%	8.7%	21.3%	10.7%
JJSF US	5.2 x	14.2 x	25.6 x	3.3%	12.9%	30.1%	11.6%
HAIN US	3.8 x	10.5 x	11.2 x	3.1%	-5.0%	22.1%	9.3%
JBSS US	5.9 x	10.7 x	18.8 x	1.5%	4.6%	21.2%	11.4%
FREE US	3.3 x	7.0 x	9.6 x	10.2%	2.3%	26.1%	14.2%
LSF US	1.9 x	n/a	n/a	-28.5%	-2.7%	14.5%	-107.8%
COCO US	7.3 x	18.3 x	26.7 x	1.4%	15.4%	36.6%	13.8%

Thesis: PetIQ should be valued like a high growth consumer packaged goods company that trades at a greater than 2x multiple than PETQ. The Company's growth model is robust, and medium term guidance of 15% EBITDA and faster earnings and cash flow growth, are well anchored. In the near term, the company's guidance and street estimates are too conservative.

1. In the short term street estimates and guidance are too conservative in the products division. There are three reasons for this.
    a. On the 4Q'23 Earnings Call, the Company noted that *"Projections bake in all the spend and none of the upside"*. Published street estimates dutifully kept their projections within the range guided.
    b. Tick and flea treatments are ~25% of the sales of the products division. The company guided for tick and flea to *revert to the mean* with expected sales below a banner 2023. So far in 2024, google trends search and nielsen data indicates that tick and flea treatment interest is as good as 2023. This indicates a better 2024 tick and flea season than expected and guided and therefore upside to both product and consolidated revenue and earnings.
    c. Nielsen data through the last week of 1Q24 also suggests pet medication is up significantly.
    d. The Products segment has organic growth potential as the existing product line expands across existing relationships and into additional regions and "inorganic" as the company introduces new products and SKUs.
2. *Short term (year end - next year)* Services margin has historically been ~20% at scale, pre-covid vs 13% in 2023. The closure of the lower margin wellness centers, in favor of community clinics

should be a very significant positive for margins in the services segment.We also believe the community clinics ramp has been guided too conservatively.

3. The Company is in the process of selling its European division, Mark and Spencer. While earnings guidance holds the division out of its future earnings, historical numbers do not, resulting in growth rates that look less robust than they actually are. Investors need to remove $700k in EBITDA from their 2023 numbers when forecasting 2024.
4. Will be below 2.5x targeted net debt/EBITDA by year end allowing additional acquisitions or share repurchases if the stock remains at these prices.

Additional Info:

Core Brands:

PETARMOR	**Flea & Tick, Dewormers, Skin & Coat Care, Ear Care, Joint Care**
CAPSTAR (NITENPYRAM)	**Flea & Tick**
SENTRY	**Behavior, Calming**
ADVECTA	**Flea & Tick**
MINTIES	**Dental Treats**
Sergeant's	**Flea & Tick, Grooming**
ESTD 2013 ROCCO & ROXIE SUPPLY CO.	**Cleaning, Training, Treats**

Additional Brands

VET IQ, PŪR LUV (LOVE · LAUGH · TREAT), foster	**Supplements/Treats**	
PETACTION, CAPACTION	**Flea**	
BUBBA'S ROWDY FRIENDS	**Cleaning**	

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As always, feel free to reach out to discuss this or any of your investments at White Brook Capital. I thank you for your support and will strive to continue to earn your trust.

Sincerely,

Basil F. Alsikafi

Portfolio Manager

White Brook Capital, LLC