MIDWAY PARTNERS
CAPITAL MANAGEMENT

midwaypartnersllc.com

January 11, 2022

Re: Calendar Year End December 31, 2021

Dear Partners:

Our Partnership has completed its first calendar year representing five months of active investing (August through December). Significant progress has been made in a short time, and the future looks increasingly bright.

We started in July with a cash pile from initial subscriptions and ended the calendar year with 14 long-equity investments representing, on a cost basis, about 78% of the total subscription capital provided by partners throughout the year. Our top five investments represented about 44% of total subscription capital on a cost basis. The gross return from our investments over the period ending December 31, 2021 was 8.7% and the net return was 7.0%. Individual partner results will vary. Please review your individual year-end account statement for specific returns.

The Partnership enters 2022 with a large cash position of about 20% of total assets. Looking forward, we would love to find one to three new investments this year where we are comfortable investing 10% or more of our total assets. Given the Partnership's focus on conservative estimates of intrinsic value and reasonable margins of safety, finding great opportunities is challenging in this environment. We remain optimistic that patience, discipline, and a large cash hedge will work in our favor over the long term, even if it drags on performance in the short term. We have no intention of selling any current holdings in 2022.

Year in Review

2021 was an exciting year for several reasons. First, we formed our Partnership in July and started investing shortly thereafter. On its own, this would make for an exciting year, but there were a few other occurrences that contributed to an interesting year:

- The ever-present COVID-19 virus and its Delta and Omicron variants
- Supply chain disruptions and entangled U.S. ports
- Semiconductor shortages
- Riots at the U.S. Capitol
- Historically low interest rates and historically lower real rates due to inflation
- Meme stock frenzies

- Continued obsession with crypto currencies and virtual assets of any kind (NFTs)
- More SPACs than we can count

Despite these circumstances, the S&P 500 set 70 new all-time highs throughout the year ending up 27% for 2021. This has only helped to reinforce the foundation of our investing philosophy, that markets are inefficient and that periods of investing exuberance and periods of investing dismay ebb and flow. 2021 was absolutely a year of unwavering exuberance as equity prices pushed ever higher. The reverse must also be true that unforeseen events that impact investor sentiment in a negative way will also occur. These will create opportunities to find investments selling at prices well below our conservative estimates of intrinsic value, just as the 2021 environment created the opposite in general. We endeavor to be patient enough and watchful enough to find them.

2022 Outlook

None. If we made a prediction for 2022, we could only be certain that we would be wrong. We prefer to evaluate individual companies but do keep in mind that equity prices are near all-time highs and real interest rates are near all-time lows. If we can identify great companies and invest at reasonable prices, accurate short-term 2022 predictions are not required to produce satisfactory long-term results.

What Not to Do

Deciding which companies should receive one's hard-earned capital and at what price is a daunting task. Even large investment funds with numerous employees and significant resources still must sift through tens of thousands of global public equity investment opportunities. Drowning in opportunities can waste valuable research time. To improve efficiency, we find it important to have a clear understanding of investments we want to avoid. These are businesses, that no matter the industry, management team, growth rate, or price we are comfortable quickly passing. We make these quick checks before we ever dive into any research. Understanding what not to do makes it much easier to find what to do. The five criteria listed below are in no particular order.

- Unfriendly to Shareholders – We avoid companies that are diluting shareholders through excessive stock option plans or other such instruments. If fully diluted shares have meaningfully increased over the past 5 to 10 years from this practice, we pass.
- Excessive Leverage – We avoid companies with large amounts of debt. We want our companies to be agile and able to weather unforeseen storms without the pressure of daunting interest payments influencing management's long-term decision making (we prefer companies with no debt). If EBIT does not cover interest expense by a wide margin, we pass.
- Inorganic Growth – We avoid companies that are serial acquirers. These companies may rely heavily on financial engineering for growth and often also fail the leverage test described above. Strategic acquisitions are important, but numerous acquisitions make us worry that management may not be treating shareholder capital with the care and discipline it deserves. If we see this pattern, we pass.

- Losses – We avoid businesses that have losses in their recent history. This includes operating losses and/or negative free cash flow. Profit may fluctuate over the years, especially in economically cyclical businesses, and reinvestment is always required to fuel growth, but we expect our businesses to make some money year in and year out. If we see a spattering of losing years, we pass.
- Industry Decline – We avoid businesses in industries with obvious disruptions (think DVDs). These businesses may look attractively priced but have declining revenues. Since the future in uncertain, it is difficult to predict the long-term pace of decline. When we encounter this type of trend, we pass.

It is important to note that none of these criteria are related to prices or growth rates or returns on capital. They are meant to be akin to symptoms presented by a new patient – they are designed to indicate when there is an underlying problem. They help reveal the mentality of how a company is operated and the strength of its underlying business. Maybe managers or boards of directors are not acting like owners or maybe the business model is fragile. Either way, these red flags indicate caution. Hold this kaleidoscope up to your future investment opportunities and see what shines through.

Investment Update

In past letters we have highlighted two large technology related investments Check Point Software Technologies, Inc. (CHKP) and Intel Corporation (INTC). In this letter, we want to highlight an investment in a small company that provides fantastic long-term prospects. Headquartered in North Carolina, Investors Title Company (ITIC) is a $375 million market capitalization business that issues title insurance policies for residential and commercial real estate.

Before we dive deeper, let's run this company through our "What Not to Do" criteria and see how it holds up.

Criteria	**ITIC**	**Grade**
Unfriendly to Shareholders	Reduced diluted share count from 2.29 million shares in 2010 to 1.89 million shares in 2021	▲ Good/ Proceed
Excessive Leverage	No debt	▲ Good/ Proceed
Inorganic Growth	Last major acquisition was in 1983	▲ Good/ Proceed
Losses	Since 1996, the only money losing year was 2008 (justifiable for a company tied to the real estate industry)	▲ Good/ Proceed
Industry Disruption	Title insurance is universally required by residential and commercial property mortgage lenders	▲ Good/ Proceed

ITIC easily passes our "What Not to Do" test. Let's move on.

The company was founded in the early 1970s by J. Allen Fine and to this day is controlled and managed by the Fine family, who combined own about 25% of the outstanding stock. We believe that the managers of this company act like owners because they are. They stand to gain, not from diluting minority shareholders, but by compounding the value of their ownership in the company. The good news is that they have done so for decades.

In general, we like the real estate title insurance business. Virtually all real estate transactions with mortgages require title insurance. The premium value is determined by the price of the property and the premium volume is based on the number of loans written. Therefore, when transaction volume goes up, premium revenue increases; when prices go up, premium revenue increases. This double-sided growth is appealing.

Most forms of insurance provide for the assumption of risk of loss arising from unforeseen events; however, title insurance is based upon loss avoidance resulting from disciplined underwriting. This has led to low loss ratios and consistent underwriting profits for ITIC.

North Carolina (36.8%), Texas (18.6%), Georgia (11.4%), and South Carolina (9.1%) are the largest sources of title insurance premium revenue. We believe the long-term real estate trends in these areas are favorable.

To determine our conservative intrinsic value for the company, we combine the value of the title insurance underwriting business profits with the balance sheet value of the company's net investment book. As of March 31, 2021 (the most recent financial information at the time of our evaluation), the company had $178 million of net investments (total investments less the reserve for claims). Isolating the underwriting profitability shows net profits of between $15 to $20 million each year from 2016 through 2019. We exclude 2020 and YTD 2021 given the booming real estate market and refinancings that are unlikely to continue at the current pace long term. Applying conservative growth rates that account for cyclicality and a satisfactory rate of return, we believe the underwriting profits are worth between $205 to $235 million. Adding this to the net investments value of $178 million and balance sheet cash of $23 million, we arrive at a conservative intrinsic value estimate for the company's equity of around $420 million or $222 per share. At the beginning of August, the stock traded at a 25% discount or $165.12 per share.

The share price closed at $197.15 on December 31, 2021. In November, the Partnership enjoyed the company's special dividend of $18 per share along with its regular quarterly dividend of $0.46 per share. The Partnership's average cost per share is $181.86. We have no intention of selling our shares should the price move higher.

We believe that we did make a mistake when investing in ITIC. Companies of this quality selling at significant discounts to our intrinsic value estimate do not come along often. We did not invest enough capital before the price moved up into a range where we are now uncomfortable adding to the position. If there is an opportunity in the future to add to our investment at lower prices, and we believe that there will be, we are prepared to do so.

Performance

As stated above, please review your individual partnership statements for performance results. As always, we caution partners about agonizing over short-term results (positive or negative). We are focused on the long-term. We are investing in high-quality companies that generate significant amounts of free cash flow. Every day more cash builds in the coffers of these companies and indirectly accrues to the Partnership. If prices fall, our investments go on sale. If the fundamental story remains the same, expect us to increase our investment size.

Conclusion

The Partnership is actively seeking new subscriptions from qualified clients. We welcome any referrals from current partners. Please contact info@midwaypartnersllc.com for more information.

As always, we are honored that you have chosen to be a part of our Partnership.

Sincerely,

Jordan Lampos

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