

## Portfolio Manager Commentary

### Second Quarter 2020

| Portfolio / Index          | Q2-20<br>Return | YTD-2020<br>Return | 2019<br>Return | Since<br>Inception |
|----------------------------|-----------------|--------------------|----------------|--------------------|
| Focused Growth Composite   | +29.2%          | +16.1%             | +37.3%         | +37.9%             |
| S&P 500 Total Return Index | +20.5%          | -3.1%              | +31.5%         | +10.2%             |
| Russell 1000 Growth Index  | +27.8%          | +9.8%              | +36.4%         | +26.0%             |

*Returns are net of fees; Since inception is cumulative*

Dear Client,

Our Focused Growth strategy delivered returns of 29.2% during the second quarter, well ahead of the broader market. If first quarter results demonstrated the importance of the quality of our portfolio and the underlying strength of the portfolio companies' balance sheets in protecting against sharp market declines from an exogenous shock, second quarter results reflect the reality that the secular trends behind which we invest are accelerating. The fact is that many of our portfolio companies are uniquely positioned to thrive in the new reality brought on by the pandemic. This is evidenced by the fact the weighted average revenue and earnings growth for our portfolio was 11% during the first quarter despite the fact that much of the global economy came to a standstill in March. As a point of reference, S&P 500 earnings were down 15% in Q1. While aggregate S&P 500 earnings are expected to decline 43% in Q2, we are confident that Q2 results for our portfolio companies will demonstrate a remarkable degree of durability.

The second quarter of 2020 marked the best quarterly return for the S&P 500 since 1998. This comes on the heels of a first quarter that saw the S&P's worst quarterly return since 2008. We are facing a global pandemic, civil unrest at home, and extreme levels of market volatility. These are unsettling times. Although it's easy to be swept away in the storm of negativity and uncertainty, the best advice we can offer is to focus on controlling the controllable. At Burke Wealth Management, this means sharpening our focus on the long-term fundamentals of our Focused Growth portfolio companies and doing our best to cancel out the day to day noise. Going forward, while we will be hoping for calmer, safer, and more peaceful times, we will continue to focus on what we can control, which is maintaining a high quality growth portfolio for our clients.

"Where's this market headed?" Without a doubt, this is the question I get asked most often with the frequency of the questions being inversely related to the recent direction of the S&P 500. In light of that, it's really surprising that after 20+ years in the industry my standard answer has typically been "I don't know," which to put it kindly is not exactly awe-inspiring. I started thinking about why this had become my standard reply. There had to be a better way to communicate the confidence I have in our Focused Growth portfolio as well as the unease I have for certain sectors of the economy, all while still acknowledging that on a day to day, week to week, or even month to month basis my guess on market direction is nothing more than that- a guess.

- 1 -

# BURKE WEALTH MANAGEMENT

I think the problem lies in the term “the market.” When pundits refer to the market, they are usually referring to the S&P 500. I’ve long been a proponent of the notion that technological innovation is accelerating the rate of change in the economy and in doing so is disrupting previously protected business models. Consequently, as a long-term investor, I want to own businesses that are doing the disrupting, or that remain insulated, and avoid businesses that are being disrupted. The fallout from the pandemic exacerbates this dynamic. On the other side of this crisis, the S&P 500 (or the “market”) is going to consist of 100 or so zombie companies that will require assistance to survive and might never reach prior levels of profitability, 300-350 survivor companies that are self-sufficient but will be picking through the rubble caused by this economic bomb and trying to chart a path to recovery, and 50 or so companies that have seen the secular trends that were driving their business accelerate and have the balance sheet strength necessary to ramp investment to meet the new reality of demand. These 50 or so companies are the pool from which we seek to source our investments. Further, fiscal and monetary policy will need to provide support to the zombie companies, as these businesses employ a lot of people and still have a great deal of economic and in some cases geopolitical importance. Think about what an extended period of 0% rates does to the terminal value of a business that is not only certain to survive, but to grow rapidly for the foreseeable future. So, to sum up, I still don’t know where “the market” is headed, but I am confident that the long-term path that our portfolio companies are on remains bright.

Trends are accelerating. This is the single biggest economic reality and opportunity coming out of Covid-19. I need to look no further than my own life to see some of the real-life changes in behavior brought on by the pandemic. My wife falls into the high-risk group, so as a family, we are taking fairly extreme precautions as it relates to the quarantine. What does this mean? First, I have been working from home for an extended period of time. This made high speed broadband a necessity and I sure was glad that my files and applications are stored in the cloud so that setting up the new home office was as easy as e-mailing log-in credentials for my virtual desktop to my laptop. Our use of e-commerce for grocery delivery went from every once in a while to almost 100%. I’ve had the same \$10 dollars in my wallet for the past three months while the number of transactions on my credit card spiked. Social media usage increased dramatically for my wife as did the time my sons spent playing their infernal video games. Finally, we even bought our own pulse oximetry device from Masimo, so we could accurately monitor oxygen saturation levels from home in the event one of us got sick. While it is usually a good idea to be leery of anecdotal tales and sample sizes of 1, I have a hunch that our quarantine experience was fairly common. Think about the major trends we just touched on: broadband connectivity, cloud computing and cloud-based software applications, e-commerce, cash to credit, social media, and telehealth. These were all massive long-term trends whose incorporation into day to day life was pulled forward by years, if not decades.

As we look out towards the macro backdrop for the next couple of months, the pandemic will continue to be a huge factor and the magnitude and severity of the recent spike in southern states will directly impact the shape and timing of our economic recovery. From a portfolio standpoint, our companies are financially strong and have remarkable agility. As such, we believe that we are well positioned for any

- 2 -

outcome. From a personal standpoint, I stand with all of you as I pray that we find a cure or vaccine as fast as possible so that the human and economic toll of this pandemic can be limited.

In addition to the pandemic, we are nearing the point where the Presidential election will begin to take center stage as investors contend with the prospects of a second term for President Trump versus a Biden administration. The pandemic is already impacting the political calendar as traditional campaigning has largely halted and the usual rollout of policy proposals has been slowed. Add into this the recent civil unrest across the country and the extreme political division that already exists and we have the makings for an unusual cycle. We will be watching closely as the respective party platforms come into focus with an eye towards sifting through which initiatives could actually be enacted versus which initiatives are simply red meat for the respective bases. Polling in a normal election cycle is very fluid prior to Labor Day and given the current macro volatility we believe that this will certainly be the case this year. Just as our portfolio companies were able to adapt to the new reality foisted upon us by the pandemic, so too will they be able to adapt to a changing political environment. To the extent legislation is passed or regulatory changes occur that degrade the long-term prospects for any of our holdings, we will make the necessary changes to the portfolio.

### **Second Quarter Notable Performers:**

Table 1 shows some notable performers during the second quarter in terms of both absolute performance as well as total contribution (% increase/decrease x weighting) to overall portfolio returns.

Table 1:

| Notable Q2-20 Performers |             |              |                     |             |              |
|--------------------------|-------------|--------------|---------------------|-------------|--------------|
| Positive Contributors    |             |              | Negative Detractors |             |              |
|                          | Performance | Contribution |                     | Performance | Contribution |
| Facebook                 | +36.1%      | +2.5%        | CME Group           | +4.5%       | +0.1%        |
| Nvidia                   | +44.1%      | +2.2%        |                     |             |              |
| PayPal                   | +82.0%      | +3.3%        |                     |             |              |

In a quarter where the portfolio delivered 29.2% returns, the available list of positive contributors to discuss was long while the list of negative detractors was quite sparse. Facebook, Nvidia, and PayPal are three positive contributors for the second quarter that warrant additional discussion. To be fair, JD.com (+49%) and Spotify (+41% since purchase) also had standout performances, but we discussed JD in last quarter's letter and Spotify will be discussed below in the portfolio activity segment of this letter. In a display of how strong the second quarter was, CME Group was the laggard of the portfolio, yet it was still

# BURKE WEALTH MANAGEMENT

up 4.5% in the quarter prior to our decision to liquidate the position to make room for more attractive opportunities.

Facebook shares were up 36% during the second quarter. To be fair, this is quite a move for a nearly \$700B company, but it is important to remember that these shares were among the hardest hit during the first quarter falling 19%. A couple of things caught our eye with Facebook during the quarter. First, Mark Zuckerberg emphasized that the pandemic had given him a renewed appreciation for running a high margin business. We think this subtle shift in communication indicates that Facebook's period of well above trend expense growth may be coming to a conclusion. More importantly, Facebook's strategy regarding the monetization of WhatsApp started to come into focus. Last fall, Facebook launched a catalogue feature to WhatsApp that allowed small businesses to post pictures and prices of their products. In April, Facebook invested \$5.7B for a 9.99% stake in Jio Platforms in India, a market with 400M WhatsApp users, with the goal of empowering 60M small businesses in India. In June, Facebook reached a deal with Visa to introduce a payments feature on WhatsApp in Brazil (WhatsApp's second largest market). WhatsApp has 2 billion global users and for the first time, we are seeing the business plan to monetize this business activated. Like the monetization of Instagram, the monetization of WhatsApp could be another powerful long-term value driver for Facebook.

Although in totality the second quarter was a great quarter for Facebook, the last week of the quarter brought unwelcome headlines as numerous well-known companies joined a boycott of Facebook initiated by a group called Stop Hate for Profit, which wanted a boycott of advertising on the Facebook platform for the month of July. Sadly, as has been the case for almost every corner of our current society, social media platforms have been unable to avoid the often vitriolic polarization of our current political environment. The key question at hand is whether the social media companies are publishers or merely platforms. Facebook has taken the position that it is a platform for the exchange of ideas and as such, not responsible for content that some may find inflammatory. The company does not want to be put in the position of constantly defining and redefining what constitutes acceptable speech. This is a situation we will monitor, but first, some facts. Facebook has over 8 million global advertisers and generated advertising revenues of ~\$70B last year. No single client represents anything close to a material amount of Facebook's business. Many brands would like greater control over where their brands appear in the platform and this has been an area of on-going dispute with Facebook. Call us jaded, but the chance to send a virtue signal to a highly interested pressure group while you reassess your advertising spending during a global pandemic seems like a pretty low risk step for a group of notoriously risk averse companies to take. We will continue to monitor this situation closely, but our sense is that this is a situation that gets worked out before any material financial damage is done.

Shares of Nvidia continued their strong run, appreciating 44% during the second quarter. Although we highlighted Nvidia as a standout performer in our last investor letter, there were two major developments at Nvidia during the quarter that warrant additional discussion. First, Nvidia's \$7B acquisition of Mellanox was finally approved by Chinese authorities. This is a glove fit deal as it pairs the world's leader in accelerated computing (Nvidia) with a leader in routing order flows through the data center. As expected, Nvidia announced that it would be keeping all Mellanox employees and increasing investment

- 4 -

immediately. These are the type of bolt-on acquisitions that we love. The second major development during the quarter was that Nvidia's next generation A100 chip set built on its Ampere architecture began to ship. This chip set represents a 20x increase in speed over the prior generation, is compatible with prior generations, and provides a single architecture that can work across all 3 major data center workloads (deep learning, cloud computing, and inference). Nvidia's accelerated computing solutions are essential to all of the major technological trends that will drive progress over the next decade.

PayPal shares soared 82% during the second quarter. PayPal's first quarter conference call was one of the more upbeat calls we've heard in recent memory. Perhaps no company benefits from the theme of trends accelerating more than PayPal as the pandemic hastened the transition towards both digital payments and e-commerce. Management was adamant that the pandemic had pulled forward digital commerce trends by years. PayPal added 7.4M users in the month of April alone. As a point of reference, the prior run rate of new users added for an entire quarter was 9M-10M. Further, the initial utilization of this new cohort of users was 30%-40% higher than historic averages. Finally, we are really excited about the long-term prospects of the recent Honey acquisition which gives PayPal the opportunity to influence consumers prior to the point of sale. PayPal is a two-sided platform that sits at the center of two massive secular trends. We increased our weighting in PayPal following the Q1 conference call.

Unlike the first quarter, their weren't too many holdings on the naughty list in Q2. Taking the metaphor a step further, had we been charged with the task, we would have delivered a lot of brand new bikes, no sticks and coal and only one pair of socks to the good little children of the portfolio this quarter. The pair of socks goes to CME Group. We sold CME group during the quarter despite appreciation of 4.5% QTD prior to sale. Unlike several prior sales, this was not driven by an egregious capital allocation decision or a complete breakdown of the investment thesis, but rather a realization that despite a period of record volatility, CME Group's results were, in our view, simply ok. We just didn't see the opportunity for a better environment for this business to excel and as such chose to reallocate those funds to businesses with superior long-term growth outlooks.

### **Second Quarter Portfolio Activity:**

Table 2 shows the changes made to the portfolio during the quarter. While overall activity was on the high side of normal, this is precisely the type of activity we hope to have. We added to PayPal, which provided an accelerating growth outlook, and initiated positions in Service Now and Spotify, which offer unique long-term growth opportunities. We sourced the funds by eliminating CME Group, which as discussed above was driven by better opportunities elsewhere as opposed to some sort of fundamental misstep. We also reduced our weightings in Electronic Arts and United Health Group, which remain core holdings but had simply enjoyed outstanding returns from the levels at which we initially increased those weightings.

Table 2:

| New Purchases / Additions |                  |               | Eliminations / Reductions |                  |               |
|---------------------------|------------------|---------------|---------------------------|------------------|---------------|
| Company                   | Beginning Weight | Ending Weight | Company                   | Beginning Weight | Ending Weight |
| PayPal                    | 4.0%             | 6.0%          | CME Group                 | 2.5%             | 0.0%          |
| ServiceNow                | 0.0%             | 3.0%          | Electronic Arts           | 5.0%             | 3.0%          |
| Spotify                   | 0.0%             | 3.0%          | United Health Group       | 8.0%             | 5.0%          |

*Individual account position changes may vary from the chart above due to various factors such as inception date or cash flows.*

**ServiceNow:** ServiceNow is a cloud-based software company that works with enterprises to transform manual ways of working into digital workflows. ServiceNow's heritage is in organizing and digitizing IT workflows onto a single, common platform with an emphasis on ease of use. Over the years, product offerings in the IT space have expanded from simple IT service management to solutions that optimize the IT operations, asset utilization, and security. Recognizing that the IT department is connected with other major functions of an enterprise, ServiceNow has added modules for use in human resources and finance.

ServiceNow is one of the vaunted "Cloud Kings". This is a group of subscription software services that are available over the public cloud. ServiceNow joins fellow cloud king Adobe in our portfolio. The Cloud Kings are all great businesses and all priced for strong future growth. Several attributes distinguished Service Now in our eyes from some of the other worthy competitors in the space. ServiceNow has 81% gross margins and 86% gross margins in its subscription software business. This suggests to us that the company has maintained pricing power as it has expanded its reach beyond its initial IT workflow focus. The cost of adding a ServiceNow subscription is usually more than offset by productivity savings for the client within the first year. This supports pricing power and explains the 98% customer retention rate. We think ServiceNow's total addressable market is substantial and expanding, which provides a long runway for continued profitable growth.

**Spotify:** Don't fire until you see the whites of their eyes. Legend has it that this famous quote came from a commander during the revolutionary war guiding his troops through a battle where they had limited ammunition. Sound strategy. I've heard this same phrase uttered periodically from investors seeking to demonstrate an aura of superior diligence. However, this is not always the best strategy. Sometimes waiting for the picture to come into full clarity comes at great cost to future returns. At Burke Wealth Management, we aspire to be like Drew Brees. We want to throw with anticipation and accuracy. The faster you see a situation developing, the greater the potential reward if you are right. That brings us to Spotify.

# BURKE WEALTH MANAGEMENT

Spotify is a global streaming audio service with almost 300M subscribers across 75 countries worldwide. The investment case on Spotify is complex and admittedly is one that hasn't quite come into clear focus. We bought Spotify because we believe this company can move beyond its current premium subscription business and build revenues from advertising on its exclusively owned content business and ultimately from independent music artists seeking placement on its curated playlists. Given the intense competitive environment in the audio streaming space, plenty of risk remains so this one could be a bumpy ride. That said, if we are correct about the development of this industry, we think this is a two-sided platform business with substantial upside.

We discussed the rationale for increasing PayPal and selling CME Group above. We also trimmed Electronic Arts and United Health Group to fund our new additions during the quarter. We had opportunistically added to both of the holdings over the last couple of years, increasing EA in late 2018 when product launch delays pressured the shares and increasing UNH last summer when the shares were depressed as the odds of Medicare for All becoming a signature part of the Democratic party platform seemed to be increasing. Both of these controversies resolved in favor of the companies and as they did, the overhang on the shares lifted. While we are not and do not aspire to be a high frequency trading organization, we do look for situations where we can opportunistically adjust the weightings within some of our long-term holdings.

2020 has been a turbulent year. There is no doubt about it. So many things have seemingly changed on a dime and the volatility that this has brought to the market has been unsettling to many. What has not changed and will not change is our strict adherence to an investment philosophy of owning high quality companies with long-term secular tailwinds. Keeping a long-term focus and understanding that the true intrinsic value of a company is not changing as wildly as the day to day swings in the stock price might suggest has been critical to our ability to navigate a challenging environment. We hope that this stability provides a sense of comfort to our investors. We thank you for the trust you have placed in us. Please do not hesitate to reach out if you have any questions or concerns.

Stay Healthy!



Ken Burke  
Chief Investment Officer

- 7 -

**BURKE WEALTH MANAGEMENT, LLC**  
**FOCUSED GROWTH COMPOSITE**  
**GIPS COMPOSITE REPORT**

| Year End | Total Firm Assets (USD) | Composite Assets (USD) (Millions) | Number of Accounts | Composite Returns Gross | Composite Returns Net | Russell 1000 Growth Index Returns | S&P 500 Total Return Index Returns | Composite Dispersion | Composite 3-Yr Std Dev | Russell 1000 Growth Index 3-Yr Std Dev | S&P 500 Total Return Index 3-Yr Std Dev | Percent Non-Fee Paying |
|----------|-------------------------|-----------------------------------|--------------------|-------------------------|-----------------------|-----------------------------------|------------------------------------|----------------------|------------------------|--|---|------------------------|
| 2020**   | 53.35                   | 39.26                             | 37                 | 16.53%                  | 16.12%                | 9.81%                             | -3.08%                             | N/A <sup>2</sup>     | N/A <sup>1</sup>       | N/A <sup>1</sup>                       | N/A <sup>1</sup>                        | 8.73%                  |
| 2019     |                         | 31.93                             | 26                 | 38.11%                  | 37.26%                | 36.39%                            | 31.49%                             | 0.31%                | N/A <sup>1</sup>       | N/A <sup>1</sup>                       | N/A <sup>1</sup>                        | 4.06%                  |
| 2018*    |                         | 7.80                              | 7                  | -13.49%                 | -13.49%               | -15.89%                           | -13.52%                            | N/A <sup>2</sup>     | N/A <sup>1</sup>       | N/A <sup>1</sup>                       | N/A <sup>1</sup>                        | 22.06%                 |

N/A<sup>1</sup> - The three-year annualized standard deviation is not presented for periods before 36 months of data is available.

N/A<sup>2</sup> - Composite dispersion is not presented for periods with five or fewer portfolios in the composite for the entire year.

\* Performance is for a partial period from October 1, 2018 to December 31, 2018.

\*\* Performance is for a partial period from January 1, 2020 to June 30, 2020.

**Focused Growth Composite:** The Focused Growth Composite is designed to deliver superior long-term returns by adhering to a simple, but proven investment philosophy. The strategy invests in high quality companies in attractive industries that possess long-term secular growth opportunities greater than that of the broader market. The strategy targets to hold a concentrated portfolio of between 18-25 stocks with initial weightings between 2%-8%. Investments are made based on projected risk-adjusted returns over a 3-5 year timeframe with a long-term focus that serves to reduce tax liability over time. The Focused Growth composite is compared against S&P 500 Total Return Index and Russell 1000 Growth Index. The S&P 500 Total Return Index is a market-capitalization-weighted index of the 500 largest U.S. publicly traded companies. The Russell 1000 Growth Index is a subset of the securities found in the Russell 1000 Index which measures large and mid-capitalization companies in the United States that exhibit growth characteristics. The Focused Growth composite was created in October 2018 and inceptioned on October 1, 2018.

Burke Wealth Management, LLC ("BWM") is a state registered investment adviser, registered with Texas and Louisiana. The firm's full list of composite descriptions is available upon request.

BWM claims compliance with the Global Investment Performance Standards (GIPS<sup>®</sup>) and has prepared and presented this report in compliance with the GIPS standards. BWM has not been independently verified.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Performance presented prior to January 2020 was achieved by the same portfolio manager while affiliated with a prior firm. The performance from the prior firm has been linked to the current composite performance in accordance with the portability requirements of the GIPS standards. Past performance is not indicative of future results.

The currency used to express performance is USD. Returns are presented gross and net of management fees and include the reinvestment of all income. Gross-of-fee returns are reduced by trading costs. Net-of-fee returns are reduced by trading costs and each portfolio's actual investment management fee. Composite dispersion is measured by the asset-weighted standard deviation of annual gross returns of those portfolios included in the composite for the full year. The 3-year annualized standard deviation measures the variability of the composite gross returns and benchmark returns over the preceding 36-month period. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

The management fee schedule is as follows: per annum fees for managed accounts are 100 basis points of the first \$5,000,000 of assets under management, 75 basis points of the next \$5,000,000 of assets under management, and 50 basis points of amounts above \$10,000,000 of assets under management.

GIPS<sup>®</sup> is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein.