EASTERN SHORE
CAPITAL MANAGEMENT
A Division of Moody Aldrich Partners

Smid Cap Equity
First Quarter 2025
COMMENTARY

Eastern Shore exploits a market phenomenon known as the **Quality Anomaly** which refers to the consistent mispricing of quality companies that leads to their outperformance over time. The strategy focuses on higher quality stocks which tend to have lower volatility and lower risk of capital loss. The strategy also invests in companies experiencing positive change in quality drivers and prefers those with long runways for future growth. Valuation discipline is used to enhance returns.

Making Waves

Smid Cap Equity Net Performance Statistics Since Inception (12/31/2012 – 3/31/2025)*

	Annualized Alpha (%)	Upside Capture (%)	Downside Capture (%)	Sharpe Ratio	Information Ratio
1 Year	-3.1	85.9	100.6	-0.6	-1.0
5 Year	-4.0	84.8	101.1	0.3	-0.9
10 Year	-0.3	89.6	94.3	0.3	-0.2
SI*	0.0	93.4	96.0	0.4	-0.1

This information is presented as supplemental to the GIPS Report, which is available **here. Statistics are calculated using net of fee performance. Net of fee performance was calculated by retroactively applying the highest model fee for the composite (.90%). Performance Statistics are calculated using the Russell 2500 index. The risk-free rate used to calculate the Sharpe ratio is the FTSE 3-month T-Bill.*

Markets/Economy

At the beginning of the new year, investors and businesses maintained optimism that the new administration would introduce a pro-growth agenda featuring an extension of the 2019 tax cuts and potentially enacting additional cuts as well. Anticipated decreases in regulations would make companies more efficient and spur M&A and IPOs. While the President was still vocal regarding tariffs, many investors assumed that new tariffs would serve as a negotiating tactic, much as they did during President Trump's first term. The nascent A.I. infrastructure buildout appeared to be a durable multi-year investment theme, enhancing the attractiveness of the opportunity set across a broad range of industries.

This relatively sanguine outlook persisted only until the end of January, when Chinese A.I. startup Deepseek announced that it had developed a low-cost A.I. model using a fraction of the computing power required by models developed by US firms. This news rattled technology stocks and brought into question how much capital would be needed to build out A.I. infrastructure here in the U.S. The assumption of U.S. dominance in the field of A.I. was also challenged given the non-U.S. firm's success in developing its model with a tiny fraction of the capital being invested by U.S. companies.

The next significant development emerged on February 1st, when the Trump Administration announced 25% tariffs on Canada & Mexico and an additional 10% on China. The President also mentioned that many product- and country-specific tariffs would be announced in the coming weeks. Market uncertainty rose as several soft economic data points deteriorated rapidly.

The March University of Michigan Consumer Sentiment Index of 57 reflected a significant decline from 74 last December. The NIFB Small Business Index dropped from 105.1 in February to 97.4 in March. The percentage of owners anticipating better business conditions dropped 16 points to a net 21%, marking the third consecutive monthly decline and the largest drop since December 2020. The Conference Board Consumer Confidence Index fell by 7.2 points in March to 92.9.

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The Conference Board's Expectations Index fell 9.6 points to 65.2, the lowest level in twelve years and well below the threshold of 80 – the level which usually precedes a recession. This soft data often precedes a deterioration in the hard economic data.

The increased volatility caused by these developments has created pockets of opportunity across our investment universe. While visibility is limited in the short term, we continue to seek out undervalued and mispriced stocks that can generate outsized long-term returns in this uncertain market.

Performance Summary *(through 03/31/2025)**

	1Q 2025	1 Year	3 Year (Annualized)	5 Year (Annualized)	10 Year (Annualized)	Since Inception† (Annualized)
	(%)	(%)	(%)	(%)	(%)	(%)
Smid Cap Equity (Gross)	-8.8	-5.1	-1.7	10.7	7.6	10.3
Smid Cap Equity (Net)	-9.0	-6.0	-2.6	9.7	6.6	9.3
Russell 2500	-7.5	-3.1	1.8	14.9	7.5	9.9
Strategy Excess Return (Gross)	-1.3	-2.0	-3.5	-4.2	0.1	0.4
Strategy Excess Return (Net)	-1.5	-2.9	-4.4	-5.2	-0.9	-0.6

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First Quarter 2025 Results

During the first quarter of 2025, the Eastern Shore Smid Cap Equity Composite delivered a return of -8.81%/-9.02% gross and net of fees, outperforming the Russell 2500's -7.50% return for the quarter.

In a reversal from the previous quarter, the Russell 2500 Value index outperformed the Russell 2500 Growth by approximately 5%. Higher quality companies – those with higher returns on equity (ROE) and returns on invested capital (ROIC) – significantly outperformed, as did stocks with lower betas. Higher market cap stocks outperformed as well, albeit by a smaller magnitude. While conditions such as these are typically favorable to our approach, the underperformance of a handful of outliers more than offset this tailwind for the quarter.

The most significant positive sector contributors to the Smid Cap Equity strategy's relative performance during the fourth quarter were Health Care and Energy. Biopharmaceutical holdings outperformed within Health Care, while outperformance in the Energy sector was driven by stock selection among oil and gas exploration and production companies.

Sector detractors for the quarter included Information Technology and Consumer Discretionary. Within Information Technology, the strategy's semiconductor and software holdings detracted significantly from relative returns. The strategy lagged within the Consumer Discretionary sector largely because of the underperformance of its sole apparel holding. The team maintained its level of exposure to these two sectors during the quarter.

The team made four significant changes to sector allocation during the first quarter: increasing exposure to the Financials sector by 5.01% and decreasing exposure to the Industrials, Consumer Discretionary, and Information Technology sectors by 6.27%, 4.27, and 2.41% respectively. No other sector adjustments exceeded 2% during the quarter. The decision to add exposure to Financials was prompted by bottom-up stock selection among non-bank financial companies, while our reduction in exposure to Industrials, Consumer Discretionary, and Information Technology holdings was driven by uncertainty with regard to tariffs and the future of A.I.

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At the individual company level, the two most significant contributors to the strategy's performance for the quarter were biopharmaceutical firm Intra-Cellular Therapies (ITCI) and specialty insurance company Palomar Holdings (PLMR). Intra-Cellular Therapies announced in January that it was being acquired by Johnson & Johnson at a substantial premium, driving the stock's price up nearly 40%. Palomar's share price jumped in mid-February on a strong earnings report and continued to rise steadily through the rest of the quarter. Additional notable contributors during the quarter included club retailer BJ's Wholesale Club Holdings (BJ) as well as biopharmaceutical holdings Verona Pharma (VRNA) and Halozyme Therapeutics (HALO). We sold Intra-cellular Therapies not long after the acquisition announcement, but we maintained exposure to the other four of these holdings as we felt that they offered additional upside.

The two most impactful detractors from the strategy's performance for the quarter were apparel and footwear producer Deckers Outdoor (DECK) and investment banking advisory company Evercore (EVR). Deckers's stock declined on tariff concerns, while Evercore's slid on concerns that uncertainty would reduce capital market activity. Other significant detractors included digital asset mining firm Core Scientific (CORZ), biopharmaceutical firm Crinetics Pharmaceuticals (CRNX), and capital markets company Jefferies Financial Group (JEF). We maintained exposure to these four holdings at quarter-end given their promising fundamentals.

From a positioning standpoint, we have maintained the balanced approach that has served the strategy well during the past two years: the strategy is not heavily biased towards growth or value, nor is it heavily concentrated or underweight in specific industries. We view the strategy as well-positioned to outperform in a volatile environment given its quality orientation and its exposure to company-specific catalysts that can offer additional upside.

Q1 2025 Top 5 Contributors†

Security	Ticker	Avg. Weight (%)
Intra-Celluar Therapic, Inc	ITCI	0.5
Palomar Holdings, Inc.	PLMR	1.6
Verona Pharma	VRNA	1.3
Halozyme Therapeutics, Inc.	HALO	1.1
BJ's Wholesale Club Holdings, Inc.	BJ	1.1

Q1 2025 Top 5 Detractors†

Security	Ticker	Avg. Weight (%)
Deckers Outdoor Corp.	DECK	1.3
Evercore, Inc.	EVR	2.0
Core Scientific, Inc.	CORZ	0.8
Crinetics Pharmaceuticals, Inc.	CRNX	1.1
Jefferies Financial Group, Inc.	JEF	1.2

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Outlook:

The degree of uncertainty regarding the global economy currently resembles that of March of 2020, when the world shut down in response to the pandemic. The path back to more normal market conditions then, as now, was impossible to predict. The difference today is that the tariffs put in place by the Trump administration can be reversed without notice.

At present, visibility into the path of inflation or economic growth is extremely limited. The dislocations in supply chains and the cost of ever-changing tariffs cannot be accurately estimated with the information currently available.

We will continue to look for and own high-quality businesses that have a reasonable path to visible growth in earnings and cash flow. Currently we are emphasizing companies with greater domestic revenues and lower exposure to products and materials that are sourced in high tariff countries. Due to the uncertainty of the path of the economy, we also own many companies that have superior revenue visibility and are less economically sensitive. We continue to scrutinize economic data, and we are engaging in conversations with company management teams frequently to gain insight into the opportunities and challenges that this environment presents to their businesses. We will remain nimble and opportunistic as conditions change.

We appreciate your interest in Eastern Shore Capital Management – please feel free to reach out if you would like to discuss any of these issues in greater detail.

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