



Wedgewood Partners First Quarter 2021 Client Letter

The Roaring '20s

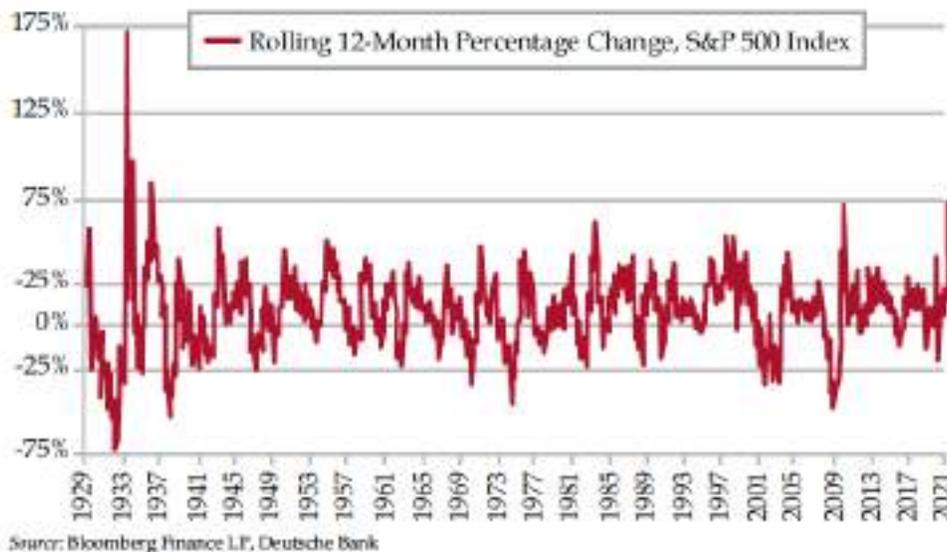
“There was a time when inflation went up, it would stay up. And that time is not now. If we saw inflation expectations moving materially above 2%, of course we would conduct policy in a way that would make sure that that didn't happen.”

Fed Chairman Jerome Powell, March 14, 2021

“And cousin, business is a-boomin'!”

Lt. Aldo Raine, *Inglourious Basterds*

S&P 500 12-Month Rolling Returns Best Since Great Depression



Review and Outlook

For the first quarter of 2021, our Composite (net)ⁱ gained +4.8%. The S&P 500 Index gained +6.2%. The Russell 1000 Growth Index gained +1%. The Russell 1000 Value Index gained +11.3%. (Note: The S&P 500 Value Index gain was the largest quarterly outperformance versus the S&P 500 Growth Index in 20 years).

Q1 Top Contributors	Avg. Wgt.	Contribution to Return
Alphabet	8.77	1.47
Tractor Supply Company	5.38	1.27
CDW	5.26	1.25
Motorola Solutions	6.43	0.71
Facebook	7.36	0.58

Q1 Bottom Contributors	Avg. Wgt.	Contribution to Return
Copart	4.12	-0.71
Edwards Lifesciences	6.79	-0.69
Apple	6.75	-0.56
Electronic Arts	4.65	-0.29
Visa	4.34	-0.20

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Top performance detractors for the first quarter include Copart, Edwards Lifesciences, Apple, Electronic Arts, and Visa. Top first quarter performance contributors include Alphabet, CDW, Tractor Supply, Motorola Solutions, and Facebook.

During the quarter we trimmed PayPal, Visa, Apple, and Edwards Lifesciences. We increased our weighting in Progressive.

We sold Bristol-Myers Squibb. We purchased Booking Holdings and Old Dominion Freight Line.

Copart reported +23% growth in quarterly operating income driven by extremely strong average selling prices (+35%) at its online salvage vehicle auctions. The Company maintains an effective duopoly in U.S. salvage vehicle auctions (along with IAA). The outsized increase in ASPs is due to Copart's unique, two-sided network platform that consists of the largest North American P&C insurance carriers and automobile dealerships, which are getting increasing access to less price-sensitive foreign salvage buyers. As automobiles are becoming more sophisticated with hard-to-repair electronics and computers onboard, Copart is helping insurance partners find a life "after salvage" with consumers, particularly outside the U.S., who place a higher value on these vehicles, often simply due to softer safety regulatory regimes. We expect Copart to grow at attractive double-digit rates as this phenomenon continues for the foreseeable future.

¹ Portfolio contribution calculated gross of fees. The holdings identified do not represent all of the securities purchased, sold, or recommended. Returns are presented net of fees and include the reinvestment of all income. "Net (actual)" returns are calculated using actual management fees and are reduced by all fees and transaction costs incurred. Past performance does not guarantee future results. Additional calculation information is available upon request.

Edwards Lifesciences business continues to generate high returns while taking market share, even as it recovers from a COVID-19-induced slowdown in medical procedures. The Company's flagship transcatheter aortic replacement valve (TAVR) franchise reported flat growth; however, this was on very difficult year ago comparisons, which saw over 40% growth in the U.S. The Company should be able to post mid-to-high teen TAVR growth this year as clinics work through a backlog of patients, and in addition, one of Edwards' competitors recently exited the market. While we reduced our weightings to fund incremental buys elsewhere in the portfolio, we continue to own Edwards as a top holding.

Apple posted +21% revenue growth to a staggering \$111.4 billion during its December quarter, plus earnings per share growth of +35%. Apple's nearly 1.7 billion active devices – 1 billion of which are iPhones – generated \$16 billion in services revenue, which was up +24% over last year. The Company has helped Corporate America adapt to a workforce that has been working from home by supplying iPhones in lieu of on-premises phones. We think the exceptional personal and professional productivity enabled by the iOS ecosystem should enable robust pricing power for years to come. As the stock has reflected more of this outlook over the past year, we have trimmed our position to fund other exceptional, though less understood, holdings.

Electronic Arts bookings grew over +18% as it benefitted from the launch of its flagship FIFA 2021, one quarter later than usual. Beyond the typical annual updates to its sports franchises, the Company did not launch any new games during its fiscal 2021 (ending March 2021). The Company (along with most large publishers) elected to add more polish to new games and generate more productivity from existing titles as the addressable market dramatically expanded during COVID-19 lockdowns. This prudent strategy should help sustain Electronic Arts double-digit gains in player count and player spend – even after the positive effects of the pandemic wane. The stock market has begun discounting the end of the Company's pandemic "benefits" as early as last summer; however, we expect the Company to be able to sustain the growth of annual titles as well as compound growth by launching new titles (such as Battlefield) on an enlarged user base.

Visa payment volume recovered along with consumer spending habits, finishing up +5% during the December quarter; but it skewed heavily toward online purchases, particularly with debit. Historically, Visa has had a meaningful portion of its volume derived from higher-yielding credit card spending related to cross-border travel and entertainment (T&E). As many countries maintain closed borders, Visa's cross-border T&E segment has stayed depressed. However, we expect this business will rebound as borders inevitably reopen to COVID-19 vaccinated populations. In the meantime, we trimmed Visa to help fund a reestablished position in Booking Holdings, which should disproportionately benefit from the aforementioned reopening as well.

Alphabet's core Google advertising business continued to reaccelerate, growing +22% during the December quarter. This rate of growth is faster than the pre-pandemic growth rates as digital advertising adoption has turned into a critical customer acquisition lifeline for businesses of all sizes in regions around the world. While this growth is hardly unprecedented at Alphabet, we are encouraged by the emerging operating leverage that the

Company has exhibited over the past few quarters. As our largest portfolio holding, we continue to expect Alphabet to significantly “under-earn” relative to its potential, often running expenses significantly higher than top-line growth, sometimes to sustain noncore, money-losing projects in its “Other Bets” segment, but also to invest in long-term opportunities such as cloud infrastructure as a service and streaming services (YouTube TV). Despite being a well-known holding in many growth portfolios, we think there is quite a bit of pent-up value in the core Google business that makes this attractive to investors of all stripes.

Tractor Supply Company reported torrid same sales growth of +27%, driven by a doubling of e-commerce sales as the Company’s rural customer base relies on it for an increasing amount of discretionary and nondiscretionary purchases, delivered more conveniently than local, regional, and national competitors. Importantly, Tractor Supply also announced the acquisition of one of its regional competitors, Orscheln Farm and Home. The Company should add significant value to Orscheln’s 167 store base by bringing in basic e-commerce capabilities, adding merchandising optimization, and helping with store modernization. We consider the vast majority of the Company’s competition to be a long, highly fragmented pool of local and regional competitors, like Orscheln, which could represent a significant opportunity for return-accretive acquisitions over the next several years.

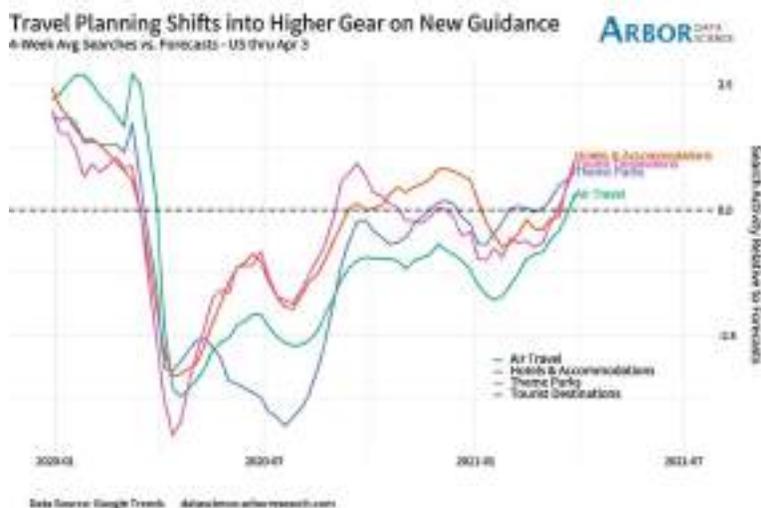
CDW returned to double-digit revenue (+10.7%) along with terrific earnings growth (+28.4%) as customers, particularly in the education and government verticals, get caught up from delayed IT spending as COVID-19 interruptions subsided in the December quarter. CDW finished the year with positive top-line growth and managed to expand margins as the Company was a critical supplier of “work-from-home” IT hardware and software solutions to small- and medium- sized businesses. The Company tends to outgrow IT spending budgets given they consistently take share from smaller distributors, while software and hardware vendors rely on CDW to generate bookings in the fragmented SMB customer channel. CDW’s tech-enabling value proposition should continue to drive reliable double-digit earnings growth, meanwhile the stock has an undemanding multiple which is why we continue to hold it as overweight in the portfolio.

Motorola Solutions saw a rebound in orders back to record levels in its North American Land Mobile Radio (LMR) business – where it enjoys a virtual monopoly – along with double-digit operating earnings growth in its software and services segment. COVID-19 posed some temporary challenges to Motorola’s selling organization; however, public service demand for more sophisticated and flexible emergency video and communications solutions stayed strong. The Company is capable of generating double-digit top-line growth as new federal spending should help expand state and local communication budgets. Despite a considerably better funding backdrop for Motorola’s largest customers, the stock trades at a multiple not too different compared to when things were not nearly as optimistic. As a result, Motorola continues to be a top holding (number 3) in our portfolio.

Company Commentaries

Booking Holdings

We reinitiated a position in Booking Holdings during the quarter. The long-term outlook for the global hospitality industry is substantially better compared to when we sold, given the recent emergence of several, well-tolerated, highly efficacious, and widely distributed COVID-19 vaccines. As vaccines are administered to a larger percent of the global population, we expect the negative trends of COVID-19 to tail off, with cross-border travel rapidly improving later in 2021 and into 2022 and beyond. In addition, the market does not appreciate Booking Holdings' formidable and competitive position in the alternative accommodations (AA) industry, particularly within the fast-growing, professionally managed subsegment of AA. Prior to the COVID-19 outbreak, the stock was trading at valuation multiples that reflected overly pessimistic assumptions about the Company's competitive positioning in the online travel agency (OTA) market. The stock has changed little compared to pre-COVID-19, and the implied competitive pressure is still much too pessimistic as the Company will play a key role in aiding properties to repopulate with customers after a dramatic drawdown.



It is a matter of “when,” not “if” the critical proportion of the global population – necessary to end the COVID-19 pandemic – becomes vaccinated. We do not know with certainty when this will happen, but we assume it will be sometime in the next year with the U.S. ahead of most developed markets. However, travelers will make plans well before this. For example, we observe U.S. hospitality search trends on Google are at never-before-seen highs. Airlines continue to post both consecutive weekly and monthly gains in air travel activity. Although the Company's offerings tend to skew more toward European hospitality, the U.S. is a good barometer for what the pace of reopening will look like once European vaccinations catch up with the U.S.

The Company ([Booking.com](https://www.booking.com)) generates the vast majority of its revenues from traditional hotels. However, we estimate that the Company is the second largest provider in the AA industry, second only to Airbnb. Despite having slightly inferior economic returns compared to traditional hotel OTA, investors view the AA industry as more attractive, particularly due to a larger and less saturated total addressable market. While Airbnb certainly has a brand-level competitive advantage in alternative accommodation compared to Booking.com, the long-term trend of alternative accommodations is toward higher commodification and increased professional management, where branding plays less of a role and conversion becomes more important. Although the trend toward professional management slowed during the pandemic, this is temporary and will resume as travel normalizes. In any case, we think Booking Holdings is capable of generating over \$4 billion in AA revenues in the next few years, which is three-quarters the size of Airbnb (which ended the quarter valued at over \$100 billion market cap). Again, alternative accommodations are only about 25% of the Company's revenues, with most of the balance of revenues coming from higher-return traditional hotels, which we would argue are more valuable than AA revenues. Given that the Company ended the quarter at a market-cap *discount* to Airbnb, we think the Company shares could double as the market realizes the tremendous opportunity Booking Holdings has in both traditional hotels and AA.

Edwards Lifesciences

We have not written about our long-term holding Edwards Lifesciences for a while, so we would like to refresh our clients on the basic story. Edwards has been driven by its TAVR platforms, which comprise roughly two-thirds of the Company's revenues, but which account for the vast majority of the Company's growth. TAVR treats a condition known as aortic stenosis, which is narrowing of the aortic valve through which the heart pumps blood into the aorta and onward to the rest of the body. This is a common condition suffered by more than 20% of Americans over age 65, according to the American Heart Association, with over 200,000 new cases in the U.S. each year. This disease does not improve on its own; once patients experience symptoms, there is a 50% risk of death within five years, and a 90% risk of death within ten years if the condition is untreated.

Before TAVR, this common problem had only one fairly traumatic solution, open-heart surgical aortic valve replacement (SAVR), which involves cracking a patient's chest open and other unpleasant activities. Understandably, both patients and doctors tended to put this option off until it was absolutely necessary. The Company's Sapien TAVR valve came along in late 2011 (today approved in 50 countries) and solved the same problem by sticking a needle in a patient's leg and threading a catheter up through a patient's body to the heart, inserting a new valve, and removing the catheter again, leaving a pinprick in the patient's leg. This remarkably antiinvasive procedure can be completed in a matter of a few minutes. So, the story here has always been 1) replacing open-heart surgery as a less traumatic option for some portion of patients with serious symptoms; and, looking more to the future, 2) treating patients, who previously would have waited for their symptoms to worsen, *much earlier* than they would be treated with surgery – solving problems before they become larger problems.

If you've followed Edwards over time, you may have noticed the use of terms like "high-risk" or "intermediate-risk" to describe the various stages of approval secured for the TAVR procedure. It is easy to become confused over this terminology. A "high-risk" patient is not sicker than a "low-risk" patient; both have severe symptoms due to their aortic valves not functioning properly. The difference is that they are at different levels of inherent risk from open-heart surgery. A high-risk patient is expected to have a higher chance of negative events (including death) due to surgery, while a low-risk patient is expected to have a lower chance of negative events. So far, government approvals in developed markets have moved from the highest-risk class of patients to low-risk patients in this most severely symptomatic patient population. Importantly, approvals for patients who are not yet seeing severe symptoms, or for patients who have impaired valve function but are so far asymptomatic, are still in front of the Company for future growth. This is the holy grail of healthcare systems around the world. Earlier intervention to prevent or delay worse symptoms or premature death in the future and allowing patients to lead healthier lives over a longer period of time. This is where we still see vast opportunity for Edwards, with a cohort of patients who may be, in large part, unknown.

We note that the market has consistently underestimated the incremental patient populations opened by each new stage of approval, from patients at high-risk from surgery through patients at low risk from surgery. In fact, we think the market continues to underestimate the available patient population for TAVR – both symptomatic and asymptomatic (the next stage of approval to come) – in current developed markets and in fledgling markets such as China, which Edwards has just entered as the first foreign company to gain approval in the market. In large part, we believe this underestimation is caused by the unquantifiable nature of much of this population. Patients whose only prior option for treatment was to have their chests cracked open generally have waited for symptoms to become quite advanced before seeking treatment, so physicians may not even know they exist yet. In other cases, patients may have seen someone in the healthcare system, but their care providers also may have counseled them against early treatment, so heart specialists are not aware of them. Edwards itself admits that it can't quantify the potential patient populations in these earlier treatment areas. We think this leads many investors to be hesitant to bet on them. Quoting the Company, patients "come out of the woodwork" every time a new TAVR center opens, and every time Edwards secures a new stage of approval.

Over our holding period, we are gratified to see the evolution of TAVR fairly closely follow our expectations. Several things have allowed TAVR to take share over time from surgery: the easing of various bottlenecks in the referral process, the expansion of new centers performing the procedure, and, most importantly, the growing library of clinical data supporting TAVR use, thus leading to a steady cadence of government approval for new patient populations. Perhaps the most important clinical data has been in the area of durability. Surgeons long tried to defend their own share by arguing that TAVR had no real durability data, and that the surgeons' work (SAVR) would prove to be more durable. However, safety studies over longer time periods, as the installed base of TAVR valves ages, continue to show comparable or better safety results versus SAVR.

The one unexpected positive during our holding period has been the recent withdrawal of Boston Scientific from the TAVR market. While we never expected Boston’s product platform (LOTUS) to be a serious competitor to Edwards and Medtronic, the two dominant players, we figured it would only be used as a specialized product in a small number of specialized indications. We did expect Boston Scientific to eventually take something like their own target of 10% share. Boston’s exit leaves a notional 5% of share to each Edwards and Medtronic (or notionally an incremental 11% in revenues for each) in this attractive and expanding market.

In conclusion, we continue to see a fairly open-ended, albeit unquantifiable, market opportunity in TAVR for Edwards Lifesciences. As clinical evidence continues to mount over a longer period, and as knowledge of the procedure continues to grow among potential patients and the physician community, we expect previously untreated or unknown patient populations to continue to appear and to lead to a continuation of positive surprises for Edwards’ fundamentals. Newer opportunities such as the Company’s recent TAVR approval in the untapped China market, or the expansion into treatments for tricuspid and mitral valves, add modestly to our attraction to the stock. Most importantly, we believe market expectations for TAVR alone remain far too conservative. While we have taken some profits on large gains recently, we still have a significant position in the stock (our 6th largest holding).

Old Dominion Freight Line

(Note: updated from our third quarter 2018 Letter)

We first bought shares of Old Dominion Freight Line in the third quarter 2018. Worried over the impact of the unfolding industrial downturn on the trucking industry, we sold the stock shortly thereafter during the second quarter of 2019. That was a mistake. We were correct to be worried about the trucking industry in 2019, but we were very wrong on how resilient Old Dominion’s business model would power through the industry downturn in 2019, as well as the Company’s exceptional performance during pandemic-laden 2020. Bucking the industry, the Company actually *grew* earnings per share by +3.8% and +11.4% in 2019 and 2020, respectively. Licking our wounds, we are shareholders once again in this terrific Company.



Old Dominion Freight Line has been a family run business for decades. Old Dominion was founded in 1934 in Richmond, Virginia by Earl and Lillian Congdon, running a single truck between Richmond and Norfolk. The founding year was fortuitous as the U.S. economy was in the early innings of its slow recovery from the Great Depression. The trucking industry boomed during the first half of the 1940s because of new congressional industry regulations and World War II armament spending.

In the early 1950s, Earl Sr. passed, and his wife, Lillian, ran the Company with sons Earl Jr. and Jack. In 1962 Earl Jr. became president. In 1962 the Company moved to High Point, North Carolina. The Company went public in 1991. In 1998, David Congdon (grandson of the Company's founders) was named President and Chief Operating Officer. In March 2018, Greg Gantt, a 24-year Company veteran was named President and COO while David Congdon became Vice Chairman of the Board and CEO.

In the ensuing decades, organic market expansion was complemented by acquisitions of Bottoms-Fiske Truck Line (1957); Barnes Truck Line, Nilsson Motor Express, and White Transport (1969); Star Transport (1972); Deaton Trucking (1979); and Carter and Sons Trucking (2001). Since 2006, trucking and transport assets were purchased from Wichita Southeast Kansas Transit, Priority Freight Line, Bullocks Express Transportation, and Bob's Pickup.

In the early 1980s Congress partially deregulated the motor carriers, granting nationwide operating authority to all applicants. In a strategic move that would emanate for years, the Company extended its services to Florida, Tennessee, California, Dallas, and Chicago, with particular focus on less-than-truckload shipping (LTL).

Trucking companies provide transportation services to virtually every industry operating in the United States and generally offer higher levels of reliability and faster transit times than other surface transportation options. The trucking industry is comprised principally of two types of motor carriers: less-than-truckload (LTL) and truckload (TL).

LTL is used for the transportation of small freight or when freight doesn't require the use of an entire trailer. This shipping method can be used when freight weighs between 150 and 15,000 pounds (think of the United Parcel Service or FedEx, but with much heavier, industrial shipments). When shipping LTL, the shipper pays for the portion of a standard truck trailer its freight occupies, while other shippers and their shipments fill the remaining space.

LTL freight carriers typically pick up multiple shipments from multiple customers on a single truck. The LTL freight is then routed through a network of service centers where the freight may be transferred to other trucks with similar destinations. LTL trucking carriers generally require a more expansive network of local pickup and delivery service centers, as well as larger breakbulk or hub facilities. Over the past few years, e-commerce has become a significant tailwind for LTL shippers.

In contrast, truckload carriers generally dedicate an entire truck to one customer from origin to destination (think of a single truck delivering Colgate toothpaste to a Walgreens distribution center). Unlike TL carriers, LTL carriers require significant capital to create and maintain a network of dense service centers and a huge fleet of tractors and trailers. The high fixed costs and capital spending requirements for LTL trucking carriers make it extraordinarily difficult for new start-ups or small operators to effectively compete with established carriers. In addition, successful LTL carriers generally employ, and regularly update, a high level of technology-based systems and processes that provide information to customers and help reduce operating costs.

The main advantage to using an LTL shipper is that shipments can be transported for a fraction of the cost of hiring an entire truck and trailer for an exclusive shipment. In addition, LTL drivers are typically paid on a per-stop basis and generally drive the same route for long periods with the added benefit that better drivers establish a rapport with customers – as well as sleep in the same bed during the week.

Over the past several years, the growth of the U.S. LTL industry has outstripped the overall U.S. trucking industry and transportation industry, in part due to a secular shift towards shorter, just-in-time supply chains, partially driven by the logistical requirements of a larger, fast growing e-commerce industry. Old Dominion has grown faster than the overall LTL market and continues to expand its profitability significantly, relative to competitors, due to its differentiated approach, which we expect will be sustainable.

According to the Company, more than 97% of the Company's revenue has historically been derived from transporting LTL shipments for its customers, whose demand for its services is generally tied to industrial production and the overall health of the U.S. domestic economy. The Company is currently the third largest LTL motor carrier in the United States, as measured by 2019 revenue with 11% of the LTL market. The growth in demand for the Company's services can be attributed to its ability to consistently provide a superior level of customer service at a fair price, which allows customers to meet its supply chain needs. An integrated structure provides customers with consistently high-quality service from origin to destination, and operating structure and proprietary information systems enable efficient management of operating costs.

The Company has been an aggressive investor in real estate and capex. Since 2011, the Company has spent over \$1.6 billion in service center additions and center expansions. Over the same time frame the Company's main competitors have not grown their collective service center capacity, while Old Dominion has grown its service center capacity by 14%. The flywheel market share-take effect of the Company's service center capacity and density has driven an increase in shipments per day by +50% to over 43,000 per day since 2011. Its competitor's daily shipments have actually declined by -5%.

As of March 2021, the Company reports that they operate 246 service center locations, of which they owned 229 and leased 17. Their network includes nine major breakbulk facilities located in Atlanta, GA; Columbus, OH; Indianapolis, IN; Greensboro, NC; Harrisburg, PA; Memphis and Morristown, TN; Dallas, TX; and Salt Lake City, UT. Service centers are

strategically located throughout the 48 states to provide the highest quality service and minimize freight rehandling costs. The Company recently announced nine new service centers would open throughout 2021. A better measure of the potential productivity of a service center is not necessarily the size (15,000 to 300,000 square feet) but the number of doors at a service center. The table below lists the Company's major breakbulk facilities.

Service Center	Doors
Morristown, Tennessee	347
Indianapolis, Indiana	318
Dallas, Texas	304
Columbus, Ohio	301
Harrisburg, Pennsylvania	300
Memphis, Tennessee	267
Greensboro, North Carolina	256
Atlanta, Georgia	225
Salt Lake City, Utah	188

Service centers are responsible for the pickup and delivery of freight within its local service areas. Each night, service centers load outbound freight for transport to its other service centers for delivery. All inbound freight received by the service center in the evening or during the night is generally scheduled for local delivery the next business day, unless a customer requests a different delivery schedule.

According to the Company, as of March 2021, the Company owned 9,288 tractors and 36,650 trailers. They generally use new tractors in linehaul operations (movement of cargo between two major cities or ports, especially those that are more than 1,000 miles apart) for approximately three to five years and then transfer those tractors to local pickup and delivery (P&D) operations for the remainder of their useful lives. In many service centers, tractors perform P&D functions during the day and linehaul functions at night to maximize tractor utilization.

Since 1988, the Company has provided the opportunity for qualified employees to become drivers through the "Old Dominion Driver Training Program." There are currently 3,069 active drivers who have successfully completed this training, which was approximately 30.3% of the driver workforce as of December 31, 2020. Its driver training and qualification programs have been important factors in improving its safety record and retaining qualified drivers. The annual turnover rate for driver graduates is approximately 6.3%, which is below the Company-wide turnover rate for all drivers of approximately 8.0%. Drivers who maintain safe driving records receive annual bonuses of up to \$3,000 per driver.



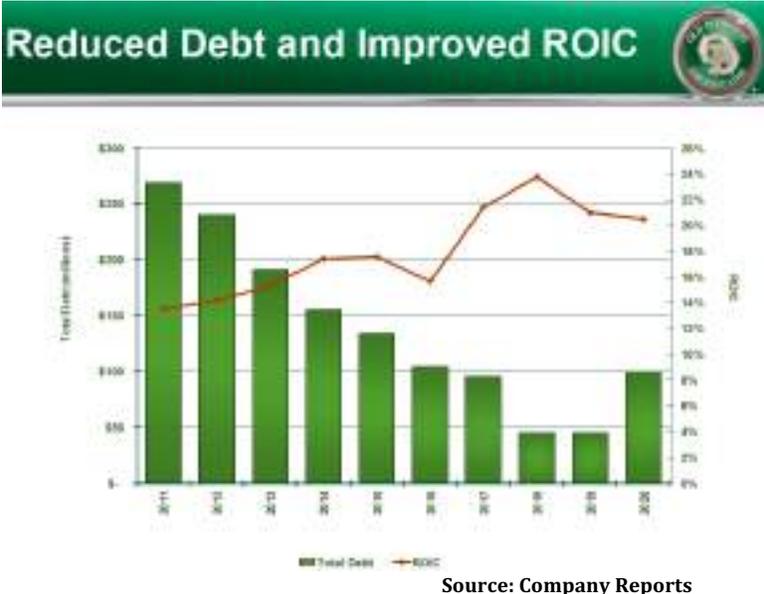
Source: Company Reports

Revenue is generated primarily from customers throughout the United States and other parts of North America with 60% industrial, 25% retail, and 15% residential. In 2020, the largest customer accounted for approximately 4.7% of revenue, and the largest 5, 10, and 20 customers accounted for 15.1%, 21.8%, and 29.7% of revenue, respectively. For each of the previous three years, more than 95% of revenue was derived from services performed in the United States, and less than 5% of revenue was generated from services performed internationally. Note the Company's declining operating ratio over the years in the graphic below. An operating ratio of 85% is the equivalent of an operating profitability margin of 15%. Old Dominion exited 2020 with an industry leading operating margin of 23.7% (76.3% operating margin).



Source: Company Reports

The Company’s long-held strategy is to grow capacity and build terminal density to ultimately get closer to its customers. Old Dominion’s competitive advantage is its industry-leading, single-integrated LTL hub and spoke network capacity, which ensures 99% on-time delivery on 1 and 2-day deliveries (70% of its daily shipments). Since 2002, on-time delivery has improved from 94% in 2002 to 99% today. In addition, the Company’s cargo claims ratio has declined from 1.5% in 2002 to just 0.1% in 2020. Relatedly, Old Dominion has been awarded the coveted industry Mastio Quality Award as the #1 national carrier for eleven straight years. Hard proof of Old Dominion’s competitive advantage is the Company’s consistent +600 basis points operating margin advantage relative to its competitors.



Annual network capex is also a Company competitive advantage to ensure industry-leading customer satisfaction. In 2021 capex should reach \$600 million – \$290 million for tractors and trailers and \$310 million in real estate and service center expansion. Note: The Company owns the real estate under most of its service centers. Such real estate zoned and purchased over the years is not only literally irreplicable, but extraordinarily valuable today too.

As noted, several of Old Dominion’s larger competitors have shrunk their service terminal networks or outsourced shipping capacity to third parties during the past decade. Meanwhile, Old Dominion has continued to expand its network of service centers and owned-and-operated linehaul and P&D tractors. As a result of Old Dominion’s consistent, long-term strategy to reinvest in capacity, the Company has substantially less reliance on purchased (third-party contracted) transportation capacity, just as the trucking industry finds itself staring down a long road of labor shortages. Historically, Old Dominion has had a low, single-digit percent of revenues serviced by third party capacity, and a few years ago moved even further away from this reliance. A limited reliance on purchased transportation allows management to focus on maximizing the profitability of Old Dominion’s existing capacity, while prudently reinvesting in incremental capacity. The Company’s focus on driving returns on owned capacity is a superior long-term strategy compared to chasing

market share, especially against the backdrop of a domestic trucking industry facing chronic capacity shortages.

We expect Old Dominion revenues to continue benefitting from the long-term shift towards LTL mode of shipping. Despite continued reinvestment in capacity to meet demand, we expect industry leading operating ratios to continue and help drive an attractive long-term, double-digit growth profile for the Company.

Starbucks

As we have observed Starbucks through the unpredictable events of the past year, we believe all the things we liked about the Company's competitive position before the pandemic have been turbocharged by the pandemic. We always have maintained the Company had no serious competition, anyway, and that in both large growth markets (U.S. and China), there was enormous fragmentation of share that would allow the Company to continue to expand through market expansion (especially in China) and through share gain versus small competitors. In fact, when we last discussed Starbucks, there was a lot of noise about competition in China from a newly established domestic competitor, Luckin Coffee, and that situation quickly dissolved into farce. In any case, had Luckin been a legitimate business, we had maintained that China was a massive market – and one in which coffee consumption was massively underpenetrated in comparison to other markets. We believed too that there was plenty of room for multiple large competitors to exploit.

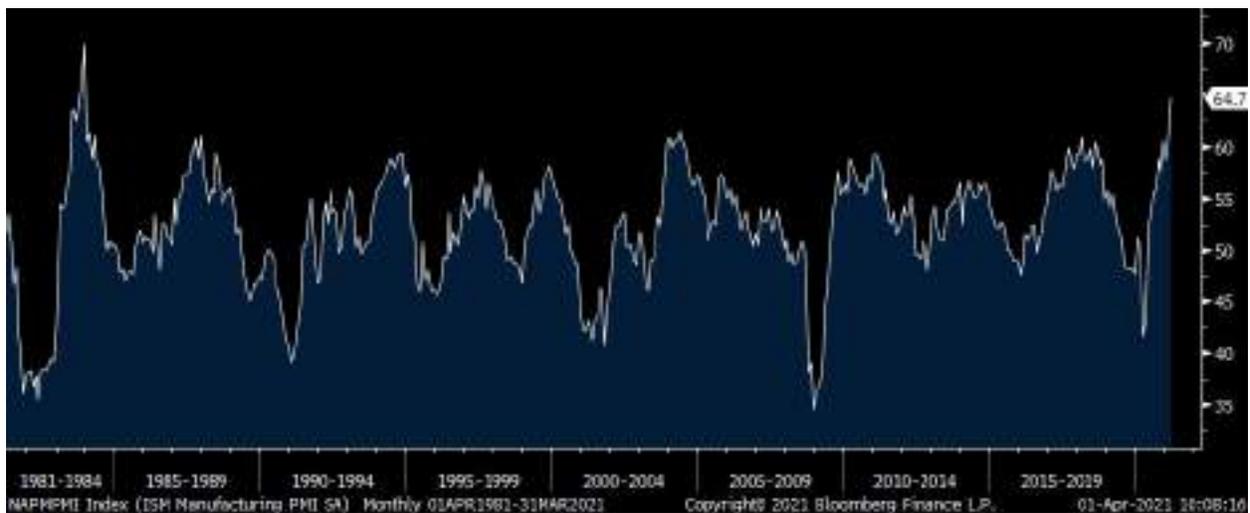
The pandemic disaster over the past year truly highlights the Company's financial strength in comparison to its small competitors, most of which struggled to survive, and many of which didn't make it. While there is no perfect data, we have seen estimates from industry groups and restaurant distributors that as many as 15-20% of small, independent restaurants across the broad food and beverage industry may have closed permanently as a result of the pandemic, sadly. Starbucks not only survived due to its superior financial position; they also used its financial resources to invest in a variety of expanded or new capabilities, including the addition of drive-through capacity, new "walk-through" pick-up locations in urban areas, increased investment in technology to drive speed within the stores and drive-through lanes, and expansion of its loyalty program. These could have been viewed, prior to the pandemic, as a fairly big advantage in terms of convenience alone versus the Company's small primary competitors. In the age of the pandemic, though, one might consider something like a drive-through an absolute necessity, as customers choose not to expose themselves to the interior of restaurants or to other people.

Another sign of the Company's superior financial strength has been the continued expansion of the store base, even in the face of the pandemic. As of the end of the Company's last fiscal year, September 2020, Starbucks had opened +4% more stores, including +13% growth in China. Additionally, Starbucks not only opened stores as competing stores folded; the Company is seeing more attractive lease terms on new stores (and on existing stores, for that matter), meaning that a store opening program that already had generated attractive financial returns will now generate even more attractive returns.

Short-term results, of course, have been quite poor all over the world, with some portion of the Company's locations closed or operating on reduced hours for the last several quarters. Customers are simply reticent to show up even when stores have been open. We expect shorter-term results to remain unpredictable, as they will be tied to the ebb and flow of various COVID-related lockdowns around the world. However, Starbucks said it expected sales at established locations in both the U.S. and China to rebound to pre-pandemic levels in the March quarter that just ended. In addition, despite reduced operating hours still, and despite customers' work and school routines being completely disrupted, a surprisingly early development in comparison to what we, at least, expected only a few quarters ago, is proof of the Company's entrenched position in its customers' lives. In contrast, the National Restaurant Association in the U.S. recently predicted that 2021 industry sales would recover significantly versus 2020, but would still come in nearly (-15%) below 2019 levels.

On the Company's most recent Analyst Day in December 2020, management took its longer-term expectations a bit higher, primarily driven by a modest expected improvement in sales versus its prior expectations. Considering smaller competitors went belly-up and the Company's investments in enhanced capabilities further improved its competitive position, we believe this improvement in longer-term sales trends is a layup. We also believe the technological investments and the improved terms from landlords create obvious benefits for to an already attractive margin and return profile. Our bullishness on the Company has not wavered and, in fact, we feel better than we did about the Company's business model over the next several years than we did when we bought the stock originally.

The Roaring '20s



The global economy continues to sharply rebound as the world enters the final innings of the pandemic. The severity of the pandemic-related economic collapse last year has led, none too surprisingly, to significant shortages across most industries. Coupled with once-in-a-

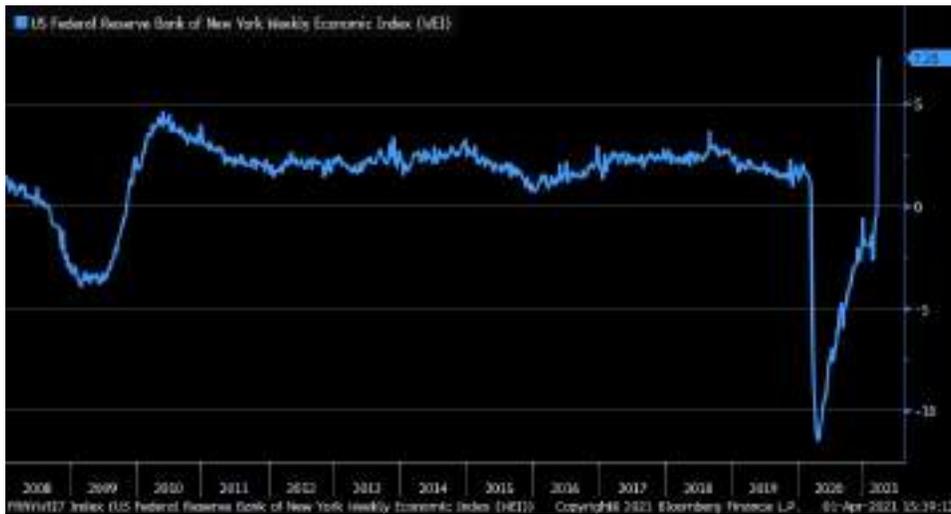
generation pent-up demand, the current breakneck pace of the current economic recovery (both manufacturing and services) is, well, once-in-a-generation as well.

Consider the following recent economic data:

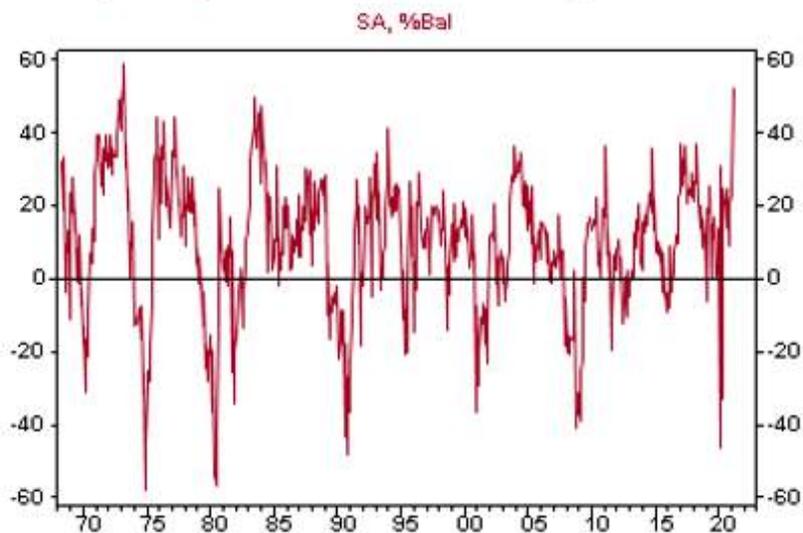
- The Institute for Supply Management (ISM) reported that the March Purchasers Managers Index (PMI) expanded at the fastest pace since 1983, with orders and production the strongest in 17 years. Relatedly, the ISM Business Suppliers Index is now at the highest level since 1974.
- ISM Services Sector recorded record growth in March as orders, hiring and prices all surged. The ISM, an association of purchasing managers, reported recently that its nonmanufacturing index rose to an all-time high of 63.7 last month from 55.3 in February, continuing a 10-month winning streak.
- The U.S. Federal Reserve Bank of New York Weekly Economic Index has gone parabolic.
- The Philadelphia Federal Reserve's business activity index jumped to 51.8 in March from 23.1 in the prior month. That's the highest reading since 1973 and crushed the economists surveyed, who expected the index to actually slip to 22. The fly in the ointment was that the prices paid index rose sharply to 75.9 in March from 54.4 in the prior month. That's the highest reading since March 1980.
- Commodity prices are boomin' along too at historic gains given the interrelated elements of unsatiated demand and supply shortages.
- Consumer confidence in the U.S. rose in March to its highest level since the pandemic started a year ago, with Americans expressing more optimism about business and labor-market conditions in the coming months.
- Consumer spending has exploded. In its most recent report on consumer spending, The Federal Reserve reported that the February consumer credit card spending reached nearly \$28 billion, which was 10X higher than expectations of "just" \$2.8 billion. Spending looks to remain robust as the second round of stimulus checks arrive soon (\$1,400 in the pockets of 285 Americans). In addition, even with the boom in consumer spending, DoubleLine reports that the savings rate, relative to disposable income, remained above the highest levels over the past 60-years. Net, net, U.S. consumers are flush with cash.
- The Conference Board on Tuesday said its consumer-confidence index increased to 109.7 in March from 90.4 in February. The reading marked the third-consecutive monthly increase. The Conference Board also noted plans to buy a house were the

highest ever since the survey began in 1967 (more inflationary supply and demand imbalances).

- Ward’s Automotive (and Quill Intelligence) reports “that U.S. auto and light truck days’ supply, the number of days needed to sell all vehicles in inventory based on the latest available sales rate, peaked at 119 days last April. This metric then quickly reversed course as many dealers, especially in the Sunbelt, never closed up shop. By May, days’ supply had been halved to 61; it remained between 50-60 through February. And then came March with a reading of 39, the second lowest in two decades. Only 2009’s Cash for Clunkers printed lower, at 29 days.”

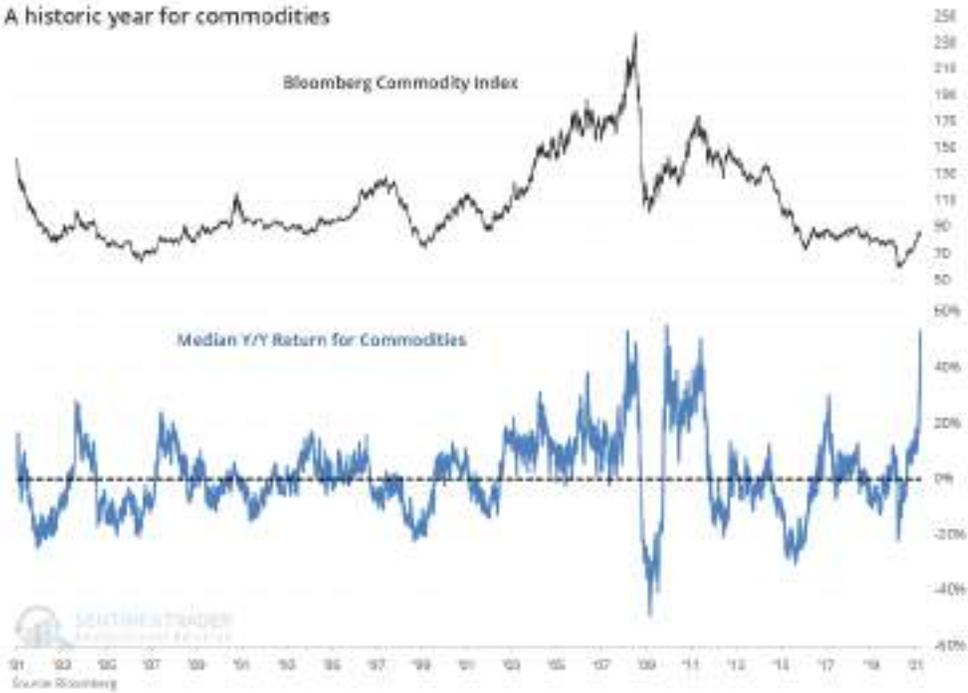


Philly Fed Mfg Business Outlook: Current Activity Diffusion Index



Sources: Federal Reserve Bank of Philadelphia and Haver Analytics; data as of March 18, 2021

A historic year for commodities



Chase consumer card spending tracker



Source: J.P. Morgan. 7-day average of total spending. Data through March 26.

U.S. Personal Savings Rate as a Percentage of Disposable Income



Figure 17: US Consumer Flush with Cash
 Since 1990, \$ in Billions, 12M Change



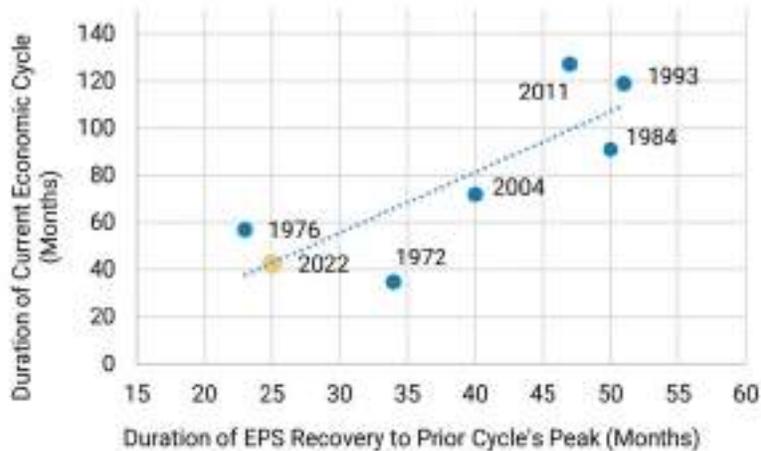
Source: J.P. Morgan US Equity Strategy and Global Quantitative Research, Federal Reserve

All told, the year-over-year first quarter GDP could exceed +10% growth and +8% real GDP for all of 2021. Coupled with inflation percolating at 2%, +10% nominal GDP growth is boomin' indeed. Once the economy fully recovers this spring from the Pandemic-led collapse last year, further economic growth should be thought of as "expansion," rather than "recovery."

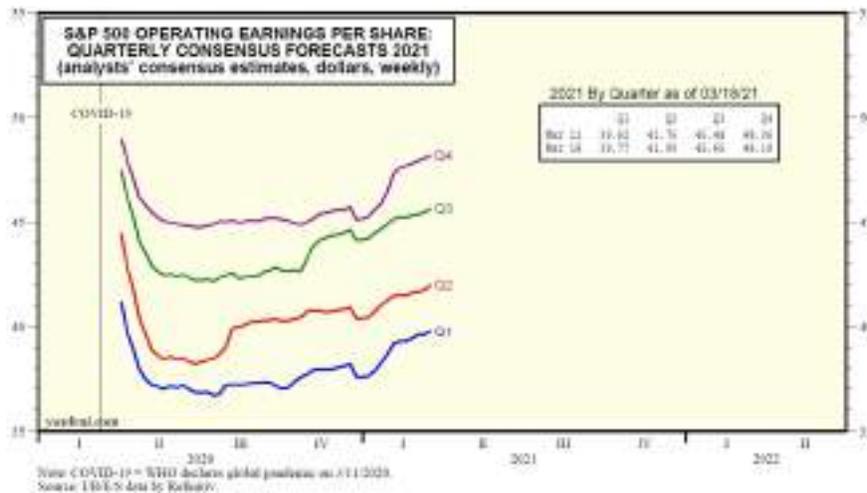
Corporate earnings are a-boomin' too. Doubly charged with margin expansive productivity gains, the S&P 500 earnings are set to increase +25% in 2021 over the depressed level in 2020. If pent-up demand proves to be stronger than expected and actually pulls demand from 2022, S&P earnings growth may exceed +30% in 2021.

Exhibit 6:

...Would Be 2nd Quickest EPS Recovery Since 1970, Implies This Economic Cycle May Be Short vs. History



Source: Bloomberg, FactSet, Morgan Stanley Research. Note: Date represents the date that peak EPS from the prior cycle was once again reached.

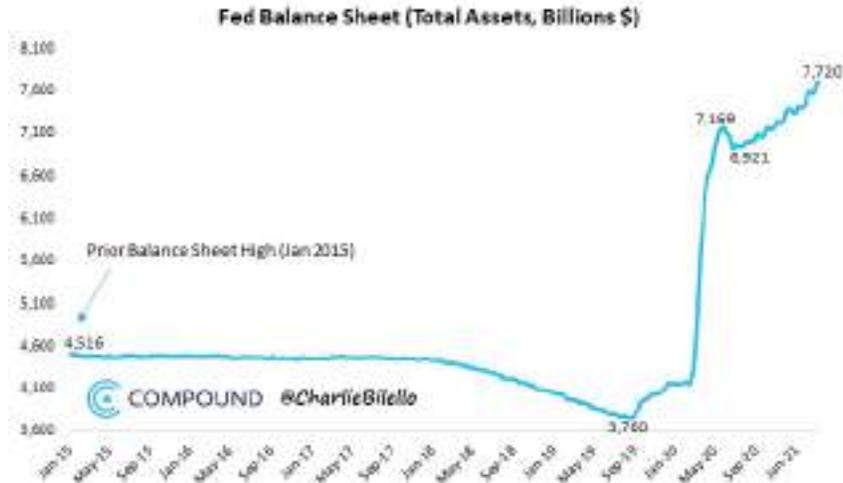


We ended our last Letter (*Trampoline or Tightrope*) opining on when, not if, the heated financial markets would force the Federal Reserve to back off of the monetary policy accelerator when we wrote this:

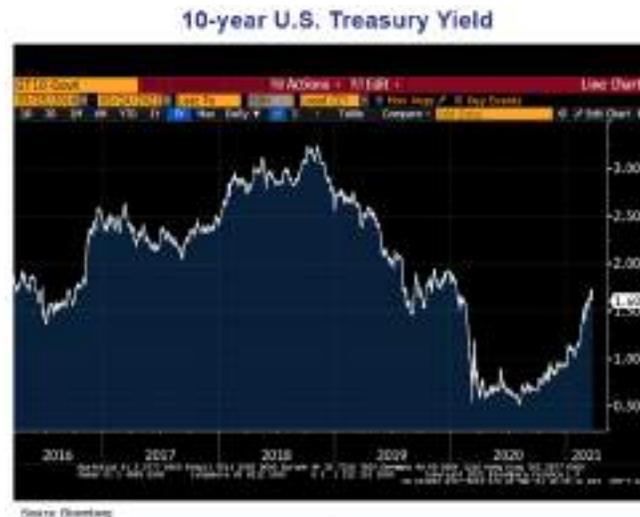
More critically still, 10-year Treasury yields have risen sharply too from just 0.50% in early August to 1.19% as of this writing. That might not seem like a big move, but make no mistake, if such yields continue to climb, then the question of when, not if, the Fed needs to change course and begin “tapering” back the size of their massive balance sheet. This emerging tightrope act for the Fed would turn The Flying Wallendas acrophobic. Add into this melodrama extremes in valuation in most parts of the stock

market, and it's an easy call to expect heightened risks for asset prices as the economy roars back in 2021. We hope Powell & Co. are already fitted for parachutes.

Over at the Federal Reserve, Powell & Co. have opined on the bubbling inflation as “transient.” Further, Powell & Co. recently reiterated their über-stimulative policy expectations that inflation will be anchored at 2%, the Federal Funds Rate will stay at zero to ¼ percent, and the continuation of their balance sheet expansion of purchasing Treasury securities and Federal agency mortgage-backed securities to the fast-lane speed of \$120 billion per month.

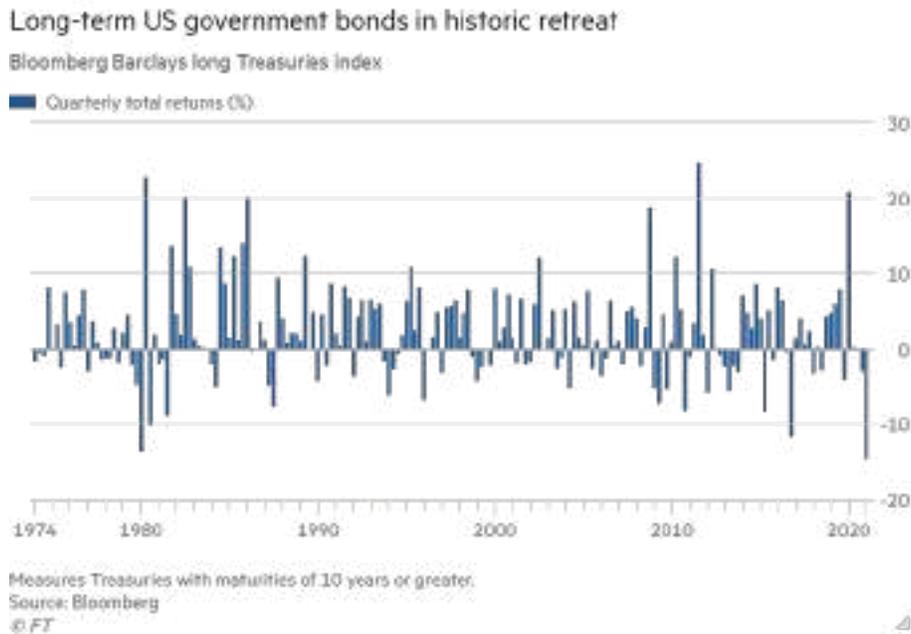
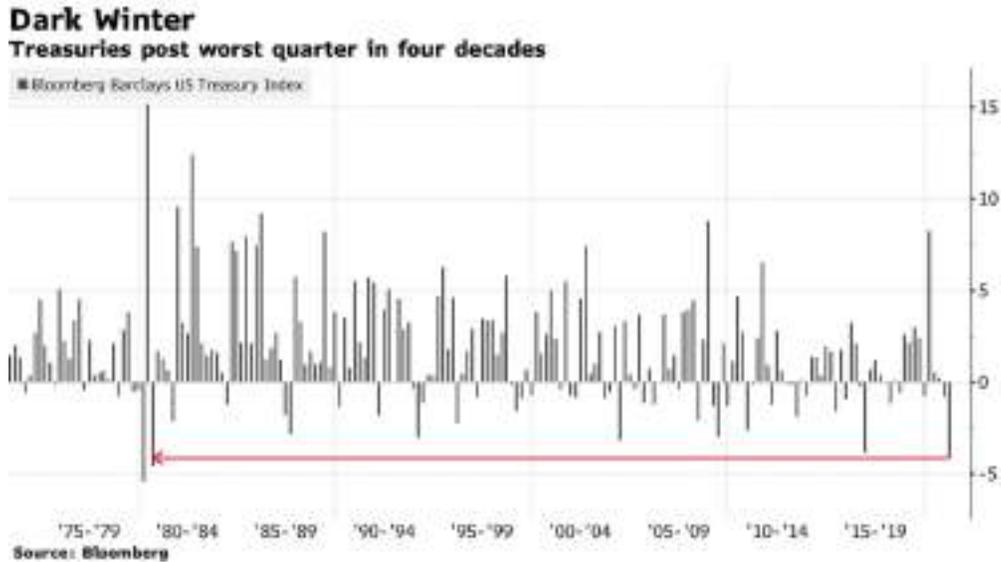


Powell & Co. remain steadfast (“anchored?”) in their policies. Markets have policies too.



The yield on the 10-year Treasury ended the quarter at 1.75%. The rise in interest rates wreaked havoc on longer duration assets. Growth stocks saw their momentum stalled, while

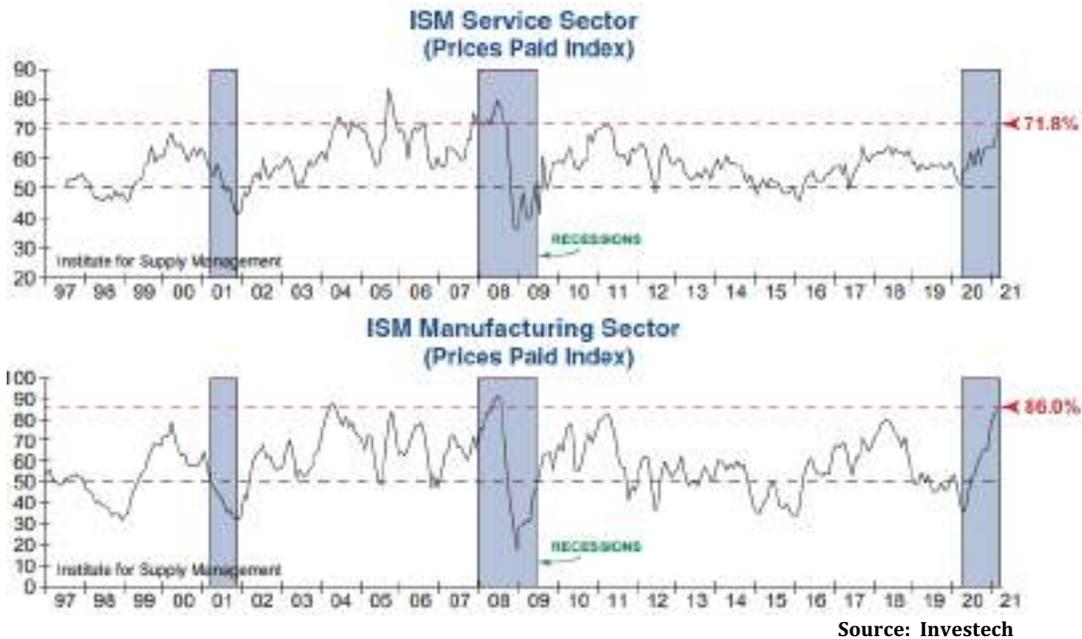
the more speculative go-go growth stocks took quite a beating. Bonds suffered, well, it was a bloodbath.



Inflationary pressures are found throughout the economy. Maybe all of the PhDs at the Fed are right. (The Fed employs more PhDs (+400) than any other U.S. institution.) Perhaps so many of the inflationary readings bubbling forth will be, well, “transient.” We have our doubts. The broad money supply in the U.S. stood at \$15.5 trillion the month before the

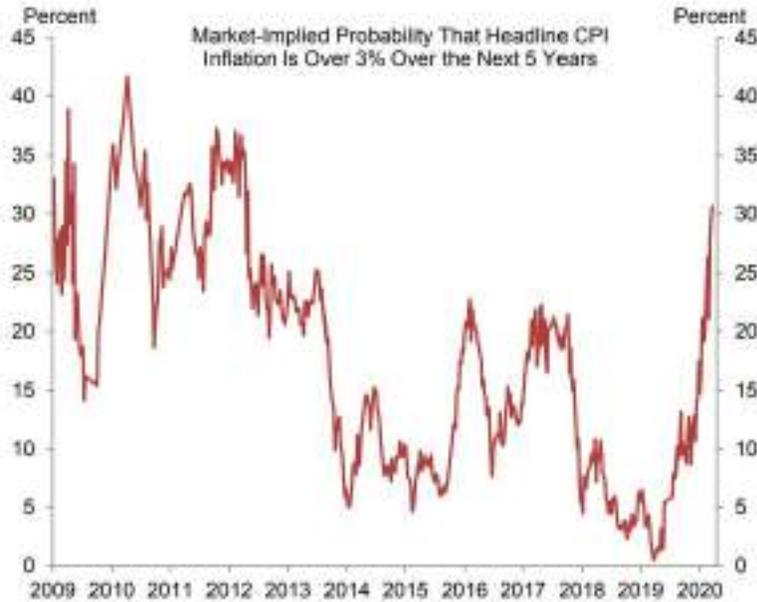
pandemic started last year. Today it is almost \$20 trillion. The U.S. economy is booming and the prices in services, manufacturing, house and condo prices, used cars, all myriad of commodities and, of course, stock prices are concomitant.

(A small sample size aside, according to Bloomberg, in Palm Beach County, across all price ranges, single-family housing contracts were up +202% last month to 1,263. Signed deals for condos totaled 1,608 – a +406% gain.)



Despite the academic firepower employed within the Federal Reserve system, Fed policy has, with rare exception, lagged the PhD firepower of the financial markets howitzer firepower

to discount the complex vicissitudes of the consumer, corporate activity, and the economy as a whole. The Fed is both forever late to take away the punch bowl – and administering hangover aspirin. If the lines in the two graphics below remain ascendant, we expect that once again the Fed will follow the markets, forcing Powell & Co. to take away their mammoth punch bowl.



Source: Goldman Sachs



Since the pandemic lows set last year on March 23, the +82% gain in the S&P 500 Index has been of historic proportions. The stock market has gripped the speculative bit with teeth

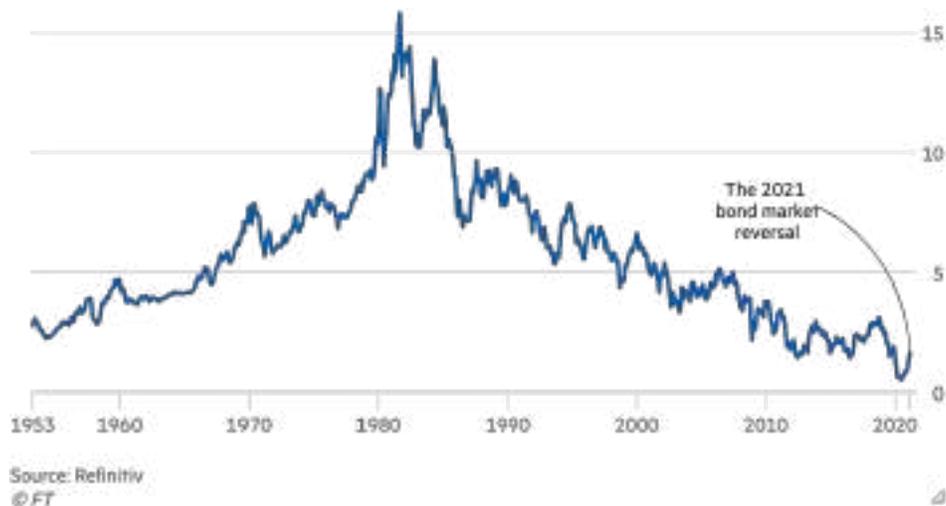
clenched (see our last [Letter](#) for more details). Such gains beg the question if the stock market, in its collective wisdom, fully discounted the worst of the pandemic, then, has the stock market fully discounted both the pandemic recovery and an economic recovery in both 2021 and 2022?

United States and Global Stocks at Extreme Overvaluation

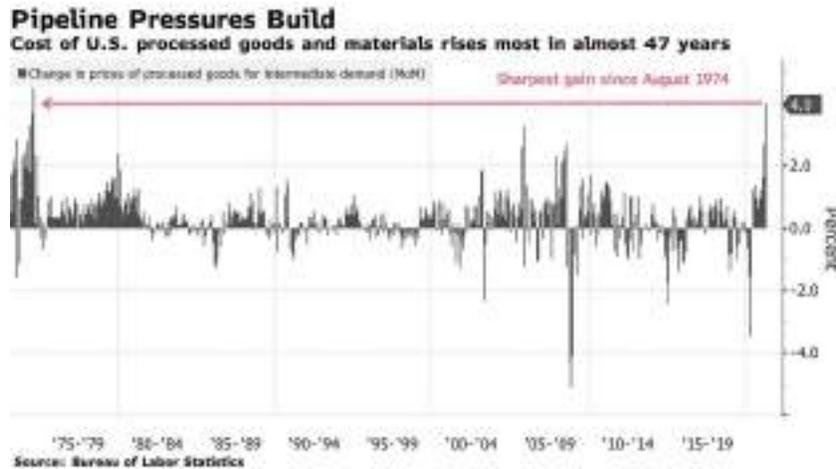


Is the recent bond reversal a blip or the start of a new fixed income market regime?

Ten-year US Treasury yield (%)



Relatedly, will the stock market begin to discount the manifold emerging signs of inflation, even without the usual inflationary tailwind of wage inflation? As of this writing, both the PPI and CPI surprised to the upside versus expectations.



We worry about both.

We would also welcome a nice, long breather in stock prices.

We wish to once again thank those clients who have been steadfast in their support of Wedgewood Partners.

April 2021

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ⁱ Returns are presented net of fees and include the reinvestment of all income. “Net (Actual)” returns are calculated using actual management fees and are reduced by all fees and transaction costs incurred.