TOWLE & CO.

July 24, 2026

To: Investors

Leadership change!

The prevailing mandate to own hyperscalers and AI infrastructure stocks at any price appears to be fading. In the first half of 2026, market leadership expanded across size, style, and sector lines: small-caps outpaced large-caps, value outperformed growth, and market breadth expanded into long-neglected cyclical industries**.**

This broadening is now visible in our performance. The Towle Value Composite ("TVC") gained 15.3% net during the second quarter, bringing year-to-date returns to 22.4% net. The Russell 2000 Value is up 23.0% year-to-date, compared with 10.2% for the S&P 500. **And the structural rotation into value has continued in July**.

With great faith in the stamina of our readership, we opted for a longer letter this quarter. We believe the evidence supporting our small cap value strategy has strengthened measurably even as risks in the broader market appear increasingly pronounced. What follows in "**The Case for Towle Value**" below is a three-part argument for reassessing current positioning and taking a fresh look at the role Towle's strategy may play within a diversified portfolio.

Performance results as of June 30, 2026, are shown below. Multi-year returns are annualized.

Periods ending 6/30/26	*TVC (Gross of fees)*	*TVC (Net of fees)*	*Russell 2000 Value*	*S&P 500*
Quarter	15.61%	15.33%	17.19%	15.20%
YTD	22.95	22.35	22.99	10.21
1 year	34.00	32.69	43.01	22.32
3 years	11.33	10.23	18.73	20.61
5 years	6.60	5.55	8.23	13.41
10 years	9.71	8.62	10.89	15.51
20 years	8.55	7.48	7.98	11.39
30 years	11.98	10.87	9.72	10.36
Inception (1/1/82)	14.64%	13.51%	11.62%	12.33%

Returns are preliminary and subject to change. Past performance is no guarantee of future outcome.
Please refer to the last page for additional disclosures.

The Case for Towle Value

"If you do not change direction, you may end up where you are heading." -Anonymous

We have organized an array of signals into three parts below. Taken in isolation, some of these signals could be explained away. Taken together, we find them impossible to ignore.

Our conclusions are as follows:

1. **Towle & Co. is better equipped for whatever comes.** We have strengthened our process, incorporated new analytical tools, and raised the standard of our work. We believe these improvements materially enhance our ability to steward capital through a wider range of market environments.

2. **Small-cap value looks unusually compelling.** After years of neglect, the segment remains underowned, attractively valued, and priced against unusually modest expectations. Encouragingly, the turn towards small-cap value may finally be in.

3. **The broader equity market appears increasingly fragile.** In our view, concentration, passive flows, valuation insensitivity, narrative-driven investing, and greater use of leverage have reinforced one another. While these conditions can persist, we believe they warrant greater caution than current market behavior would suggest.

Part I. Progress at Towle
Building and Using Better Tools

"The only antidote for being an absolute klutz due to the presence of man-with-a-hammer syndrome is to have a full kit of tools." -Charlie Munger

We are pleased with our year-to-date results and believe recent enhancements to our systematic value process deserve much of the credit.

Forty-five years of valuation-focused investing have carried us far on one tool. That need not be the only tool that takes us forward. Even the best hammer is better with a wrench beside it. Valuation will forever remain our anchor, but cheapness alone does not distinguish between a company nearing an inflection point and one whose problems remain unresolved.

Here is what we've built and implemented of late:

- **Market Traction**: In our first quarter letter, we introduced **VALT (Value + Traction)**[1], our proprietary tool for ranking stocks within our valuation-based opportunity set. VALT blends Towle valuation measures with volatility-adjusted momentum, which we refer to as traction. We believe VALT has strengthened several important elements of our investment process:

  - **Objective:** Focus capital where attractive valuation, improving business fundamentals, and market validation are converging.

  - **More Disciplined Entry Points:** Valuation identifies what may be mispriced; fundamental research tests the business case; traction helps determine when the evidence is strong enough to commit. We do not want capital trapped in stagnation.

  - **Stronger Portfolio Management:** Every holding must continually compete for capital. VALT helps rank the opportunity set and informs research priorities and position sizing. Higher-ranked ideas can earn more capital; lower-ranked holdings must justify their place against stronger alternatives. The relevant question is not where we bought the stock, but where the best forward return now resides.

  - **Greater Sensitivity to Opportunity Cost:** VALT will occasionally produce false negatives, including full exits ahead of eventual recoveries. We accept that trade-off. In our judgment, the more consequential risk is allowing cheapness to justify prolonged stagnation while stronger opportunities pass us by.

  - **In Good Company**: Cliff Asness, James O'Shaughnessy, and Wesley Gray (among others) have published extensive research on the benefits of combining value and momentum. Our approach adapts that established principle to Towle's unique discipline – emphasizing EV/Sales, earnings potential, and volatility-adjusted momentum to build a more robust measure of "traction" rather than relying on simple price momentum alone.

  In sum, VALT is designed to sharpen our entries, tighten portfolio management, help us hold winners longer, miss fewer opportunities, and keep capital from getting stuck in stagnant positions.

- **Artificial Intelligence**: The progress of AI models in the last year has been incredible for investment research. AI tools now support the Towle investment team in drafting deep-dive investment memos, providing skeptical feedback, and gathering information at a pace and depth we could not achieve otherwise.

Our conclusion: While we make no assurances regarding future investment outcomes, we believe Towle is better equipped than ever to invest successfully across a full range of market environments. AI is improving research efficiency and allowing our portfolio managers to devote more time to underwriting, portfolio construction, and judgment-intensive decisions, while VALT is strengthening stock selection and entry/exit discipline.

Part II. Supporting Evidence
Value and Small-Caps

"To think is easy. To act is difficult. To act as one thinks is the most difficult of all." -Johann Wolfgang Von Goethe

- **Extreme Valuation Discount**: On Strategas' data, the forward P/E of the small-cap S&P 600 relative to the S&P 500 sits roughly a standard deviation below average, a discount last seen around the turn of the millennium:

- **AI Beneficiaries**: The first phase of AI seemed to reward whoever sold the scarce ingredient; the next phase likely rewards whoever uses it. For the real-economy stocks in the Towle portfolio, much of the potential lies in the work behind the work:

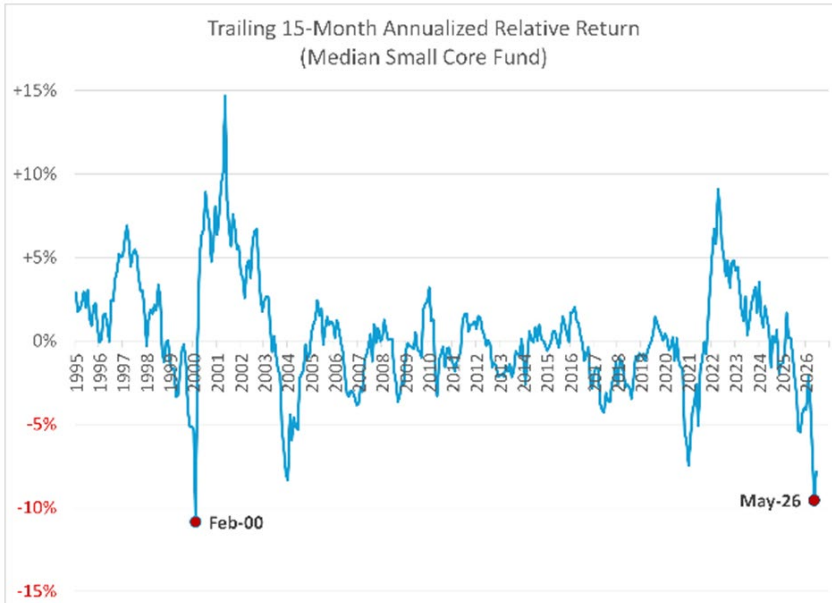
  - scheduling and dispatch;
  - purchasing and inventory management;
  - billing, claims and collections;
  - compliance and document processing;
  - customer service;
  - approvals and exception handling;
  - and back-office reconciliation.

  These activities consume substantial time and expense. Manufacturers, distributors, field-service providers, and logistics companies often carry entire layers of employees whose primary role is coordinating other work. AI gives these companies a new way to attack costs previously treated as permanent.

- **Jevons Paradox**: William Stanley Jevons observed that increased efficiency of coal engines paradoxically led to *increased* coal consumption.[2] When a good or service gets cheaper, we tend to demand and produce *more* of it. Torsten Slok of Apollo applies Jevons to today and says it is entirely possible – perhaps even likely – that AI will serve to *increase* hiring demand. This is bullish for the broad economy.[3]

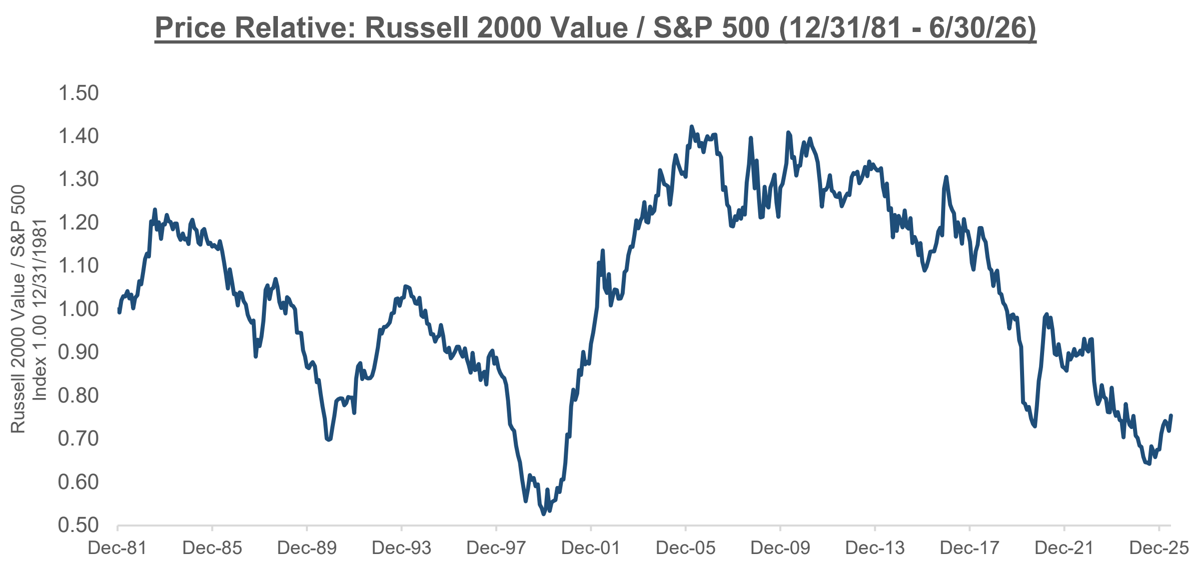
- **Charting Lows**: In “NOW IS THE WORST TIME TO FIRE YOUR SMALL-CAP MANAGER,” (all-caps not our emphasis) Furey Research Partners notes that the median small-core fund is running nearly 1,000 basis points per year behind its index since March 2025. This is the worst stretch since early 2000. Historically, that kind of extreme has marked a setup for dramatic mean reversion:

Fig. 1. **We are undoubtedly in one of the worst 15-month periods for small-cap managers**



Source: FRP, FactSet, Morningstar; as of 6/30/26, Performance in periods longer than 12 months is annualized

- **Small-Cap Value Performance Basing**: The ratio of the Russell 2000 Value index to the S&P 500 has fallen to the lowest levels since the late 1990s, but may be recovering:



Source: Towle & Co.

Our conclusion: The conditions favoring small-caps and value have been developing for several years, but the inflection point may just now be in the rear view. Relative valuations remain compelling, recent performance has strengthened, and the benefits of technology and innovation should extend well beyond the market’s largest companies. In our view, the balance of evidence increasingly supports a meaningful allocation to small-cap value.

Part III. The Other Side
Leverage, Concentration, and Froth

"What we learn from history is that we do not learn from history." -Benjamin Disraeli

- **Record Concentration**: Diversification may be the only free lunch in investing, but investors aren't getting it in today's S&P 500. Semiconductor stocks reached ~20% of the S&P 500 at quarter end, about four times their 2020 weight and more than double their share at the dot-com peak. The top 10 holdings in the S&P 500 are nearly 40% of the index. A market index that appears diversified by company count has become increasingly dependent on one investment theme. How did we get here?

- **Passive Herding**: Citadel Securities' Scott Rubner describes the passive investing loop as self-reinforcing: if a stock goes up, its weight goes up, which forces passive funds to buy still more of it.[4] This can "work" if the wisdom of crowds holds.

- **(Arguable) Stupidity**: In "How crowds become stupider,"[5] the Financial Time's (FT) Stuart Kirk reminds readers that the wisdom of crowds depends crucially on the independent guesses of participants. "The wisdom of crowds has never lain in the consensus. It lies in the disagreement. Once everyone thinks alike, crowds are error-prone." Passively outsourcing investment decision-making to the crowd may have made sense when passive assets were a small minority of the market. But passive fund assets surpassed active more than two years ago.[6]

- **Korean Margin Calls**: In South Korea, roughly 1.2 million leveraged retail accounts hit margin calls in a single mid-July stretch, with more than 320,000 fully liquidated, as the KOSPI fell over 25% from its June peak.[7]

- **Chinese Life Support**: A cheap, open-source Chinese model (Moonshot's Kimi K3) helped trigger a global chip selloff[8]; over the following weekend, two Chinese-state-backed funds deployed about $9 billion into equities and ETFs to stabilize prices.[9]

- **Record Margin Leverage**: According to Hussman Strategic Advisors[10], domestic margin debt hit a record $1.4 trillion in May. Near 4.4% of GDP, this is the highest reading in over half a century:

- **Private Credit Refusals**: Blackstone and Apollo both capped redemptions for their popular credit funds at 5% this quarter after double-digit withdrawal requests[11].

- **AI Pricing Power**: A real-time gauge of AI spending (the Silicon Data Token Expenditure Index) has rolled over from record highs.[12] And on the All-In podcast, Google Ventures founder Bill Maris argued that deeppocketed incumbents like Google should dramatically cut prices to squeeze profit-poor rivals such as OpenAI and Anthropic. That threat is compounded by cheap Chinese open-source models.

- **OpenAI's Profit Problem**: Unsurprisingly, given the above, OpenAI's leaked 2025 financials show roughly $13 billion of revenue and a ~$21 billion operating loss. And yet, the company has "committed" to some $1.4 trillion of future spending. Logical next stop? Washington. As reported recently by the FT[13], OpenAI is in discussions to give a five percent equity stake to the US government.

- **Stalled Leaders**: Even after a strong second quarter, the "Magnificent Seven" are trailing the S&P 500 year-to-date. Perhaps it's the capital spending. Hyperscaler AI capex plans are off the charts. In our experience, competitive capital spending is how industries create overcapacity and destroy long-run profitability.

Our conclusion: Investors should approach the S&P 500, Nasdaq, and other concentrated large-cap exposures with heightened caution. The Nasdaq took approximately 15 years to regain its prior peak following the technology bubble, underscoring that valuation and concentration risks can take considerable time to resolve. Against today's backdrop of elevated leverage, passive ownership, narrow leadership, speculative excess, liquidity concerns, and geopolitical uncertainty, the recent weakening of market leaders may warrant a reassessment of portfolio exposures and a selective rebalancing of capital.

Quarterly Portfolio Review

Top contributors this quarter came from electronic components, technology distribution, healthcare, and real estate. Leadership did not simply rotate from one narrow theme to another. It spread across industries and investment narratives. The detractors in the quarter were more traditional value stocks that supported first quarter performance – materials, industrials, and some staples.

Notably missing from our contribution table below are energy stocks, an overweight sector group we have been carefully trimming as the conflict in Iran continues to drive volatility in the energy space. As of this writing, our two remaining refiner positions sit near all-time highs while the pressure pumpers (with new power generation exposure to the AI buildout) are off their highs.

Below are the largest contributors and detractors to quarterly performance (as measured by contribution to return):

	Company	Contribution %		Company	Contribution %
1.	Methode Electronics (MEI)	3.88%	1.	Alpha Met. (AMR)	-0.57%
2.	Oscar Health (OSCR)	2.89%	2.	AdvanSix Inc. (ASIX)	-0.53%
3.	Molina Healthcare (MOH)	1.56%	3.	Oshkosh Corp. (OSK)	-0.46%
4.	TD SYNNEX (SNX)	1.51%	4.	PVH Corp. (PVH)	-0.39%
5.	Compass, Inc. (COMP)	1.45%	5.	Bunge Global (BG)	-0.37%

Past performance is no guarantee of future outcome. The contribution to return characteristics shown do not reflect the deduction of all fees and expenses that a client has paid or would have paid. Please refer to the total composite gross and net performance on page 1 of this letter to understand the overall effect of fees over the same period. Refer also to the last page for additional disclosures.

Looking Ahead: A Broadening Market

In our view, the next phase of the stock market is unlikely to be defined by a simple, uniform rotation from large companies to small ones or from growth to value. Market leadership is likely to broaden unevenly, favoring companies where low expectations intersect with AI-driven productivity gains and improving business conditions. That is precisely the distinction VALT is designed to identify.

Several conditions that have historically supported strong periods for small-cap value stocks may be aligning:

- **Resilience in inflationary periods.** According to Strategas, small-cap equities have outpaced inflation in every decade since the 1930s. In an environment where inflation may remain less benign than in the prior cycle, that record supports the case for owning economically sensitive businesses with pricing power, operating leverage and exposure to nominal growth.

- **Wide dispersion and low expectations.** Valuation spreads between market leaders and small caps remain near historic extremes. Many small-cap value companies need only to modestly exceed depressed expectations.

- **Changing monetary regime.** A Kevin Warsh-led Federal Reserve may place greater emphasis on balance-sheet restraint, AI-related productivity gains, and supply-side growth. A less interventionist policy framework could benefit rate-sensitive, cash-generative companies versus long-duration peers.

None of these conditions guarantees a straight-line advance, but valuations in our universe remain attractive, expectations remain modest and leadership is beginning to move beyond the companies that dominated the last cycle. **As the market becomes more selective, we believe the advantage will shift from owning what has already worked to owning what is beginning to work.**

We are heavily invested alongside you, with firm and employee capital representing over 20% of assets under management at quarter end[14]. For long-term investors seeking to diversify beyond crowded market leaders, we believe the greater risk is waiting until broader participation is fully evident and the relative valuation opportunity in small-cap equities has materially narrowed.

Thank you for your continued partnership. We welcome your comments and feedback at info@towleco.com.

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DISCLOSURES: 1) Towle Value Composite performance results are calculated using a time-weighted total-rate-of-return method and are expressed in U.S. dollars. Results include the reinvestment of all income. Gross of fee performance is presented as supplemental information and reflects the deduction of all trading expenses, except in those accounts where ABP (Asset-Based Pricing) fees are assessed in lieu of standard trade commissions. Net of fee performance was calculated using actual management fees and ABP fees. 2) Although Towle & Co. makes no attempt to manage against the composition of a specific benchmark, the Firm provides the Russell 2000 Value Index as a readily accessible indicator of comparative small cap performance as well as the S&P 500 Index as a general indicator of the market at-large. The performance of an index is not an exact representation of any particular investment as one cannot invest directly in an index and investments made by Towle & Co. differ in comparison to the Russell 2000 Value Index in terms of security holdings and industry weightings. Towle & Co. invests in considerably fewer companies than either index with lower average multiples to book value, sales, earnings, and cash flow, and as a result, the volatility and returns of the indexes may be materially different from the individual performance attained by a Towle & Co. investor. 3) Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Unless otherwise noted, references to 'the Towle Portfolio' or 'the Portfolio' refers to a representative, fully discretionary portfolio managed in the Towle Value strategy and member of the Towle Value Composite. Contribution to return is a performance attribution characteristic that measures how much an individual asset, sector, or portfolio component contributes to the overall portfolio return. Information regarding the methodology used to calculate the contribution to return for Portfolio contributors and detractors and a report showing the contribution to the Portfolio return for each security in the Portfolio are available upon request. 4) The companies identified and described in this communication are intended to illustrate certain concepts employed by Towle & Co. in the management of its Value strategy. The companies identified do not represent all of the securities purchased, sold or recommended for client accounts and certain data, such as the purchase price, sell price, or holding period return may not be indicative of an individual client's actual experience. The reader should not assume that an investment in the securities identified was or will be profitable. 5) Under no circumstances does the information contained within represent a recommendation to buy, hold or sell any security. Towle & Co.'s opinion of a company's prospects should not be considered a guarantee of future events. Opinions expressed are those of Towle & Co. and should not be considered a forecast of future events or a guarantee of future results. Opinions and estimates offered constitute our judgment as of the date set forth above and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. All material presented is compiled from sources believed to be reliable, but no guarantee is given as to its accuracy. 6) CFA® is a designation issued by the CFA Institute. To earn the designation, candidates must pass three course exams, each requiring approximately 250 hours of self-study, and have completed four years of qualifying work experience.

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[1] The VALT score is an important metric in Towle's investment screening and decision-making process. However, it is not a guarantee of effectiveness, or security-level or portfolio performance. The information in this communication is provided to illustrate certain concepts related to our use of the VALT score. Momentum / volatility signals can fail and can underperform. No assurance is made that objectives will be met.
[2] William Stanley Jevons, The Coal Question (London: Macmillan, 1865)
[3] Apollo, April 28, 2026, "The Jevons Employment Effect From AI," Torsten Slok
[4] Investing.com, June 30, 2026, "Chip stocks hit record 19.7% of S&P 500, quadrupling since 2020," Frank DeMatteo
[5] The Financial Times, July 3, 2026, "How crowds become stupider," Stuart Kirk
[6] Morningstar, January 17, 2024, "It's Official: Passive Funds Overtake Active Funds," Adam Sabban
[7] Reuters, July 20, 2026, "Korean stock volatility comes to America. Can Wall Street take the heat?" Jamie McGeever
[8] Wall Street Journal, July 17, 2026, "China's Moonshot AI Adds More Fuel to Wall Street's Chip Selloff," Vicky Ge Huang
[9] The Financial Times, July 20, 2026, "China's 'national team' buys shares worth $9bn to prop up market," William Sandlund
[10] Hussman Funds, July 2026, "Mountain, Cliff, or Ocean," John Hussman, Ph.D
[11] CNBC, June 23, 2026, "Apollo curbs withdrawals after exit requests hit 17%, reigniting fears over private credit liquidity," Hugh Leask
[12] Bloomberg "Points of Return," July 6, 2026, "A token grasp of the AI boom shows trouble brewing," John Authers
[13] The Financial Times, July 1, 2026, "OpenAI proposes handing Trump administration 5% stake," Cristina Criddle
[14] Calculated as of 6/30/2026 using the sum of all firm and employee client accounts as a % of total firm assets under management.