Cooke & Bieler

Q3 2023

Mid Cap Value Equity

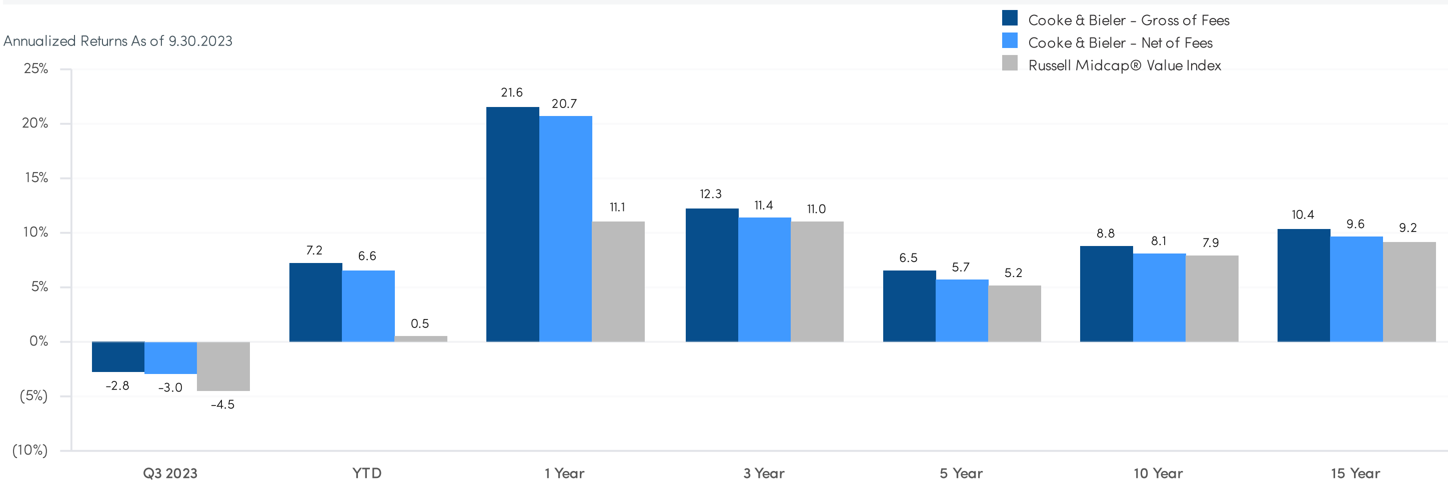
Overview

Markets continued their upward trend early in the third quarter, though rising oil prices and the prospect of persistently higher interest rates ultimately sapped investor optimism and pushed major indices down modestly for the full three-month period. The S&P 500® lost 3.6%, the tech-heavy NASDAQ fell 4.1%, and the Russell 2000® Index declined 5.5% as small caps lagged their larger counterparts. Energy was the best performing sector across the board, fueled by a 28% rise in WTI crude. Conversely, yields on 10-year Treasuries rose by nearly 90 basis points to their highest levels since 2007, sending the yield-driven Utilities and Real Estate sectors lower. Perhaps not surprisingly, mounting economic anxiety seemed to benefit stocks of higher quality businesses, as evidenced by the outperformance of companies with higher returns on capital and lower debt leverage.

Portfolio Performance & Developments

Cooke & Bieler's Mid Cap Value Strategy outperformed the Russell Midcap® Value Index for the fourth consecutive quarter, posting a -2.84% return gross of fees (-3.02% net of fees) against a -4.46% return for the Index. Outperformance was primarily driven by positive stock selection effect, though sector allocation effect was also beneficial. Portfolio holdings within the traditionally cyclical Consumer Discretionary and Industrials sectors – particularly American Eagle Outfitters and ESAB – performed best despite ever present recession fears. Communication Services and Financials holdings were also additive. Partially offsetting these results were Information Technology holdings such as Open Text Corporation and MKS Instruments, as well as the portfolio's Health Care holdings.

Mid Cap Value Equity Composite Performance



Source: FactSet and Russell®

Past performance is not indicative of future results. All investing involves risk, including loss of principal.

Click for additional C&B Mid Cap Value Performance Disclosures

Mid Cap Value Equity

Five Largest Contributors/Detractors

	Avg Weight (%)	Net Total Return (%)	Net Contrib. to Return (bps)
American Eagle	1.6	41.8	50
Fidelity National Fin.	2.4	15.8	31
Warner Music Group	1.7	20.8	27
Gentex	2.8	11.5	27
Helen of Troy	3.2	7.7	22

	Avg Weight (%)	Net Total Return (%)	Net Contrib. to Return (bps)
Omnicom	2.5	-21.2	-55
Teleflex	2.1	-18.9	-43
Discover Financial	1.5	-25.5	-40
Open Text	2.5	-15.2	-39
CarMax	2.3	-15.7	-38

Source: FactSet

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Largest Contributors

American Eagle Outfitters (AEO), a leading retailer of teen and young adult apparel, was the largest contributor. Having lowered expectations earlier in the year in response to an uncertain consumer environment, AEO reported better than anticipated sales and margins for their fiscal quarter ending in July. This progress enhanced the credibility of management's longer-term growth and margin targets and boosted optimism for this year's holiday season.

Fidelity National Financial (FNF), the largest U.S. title insurer, was the second-largest contributor. FNF's title revenue fell sharply year over year as higher interest rates depressed mortgage activity. The company's strong cost control, however, allowed them to produce better than expected margins while their annuity subsidiary posted strong sales results. Additionally, sentiment was undoubtedly aided by hopes that interest rates may have peaked.

Warner Music Group (WMG), the world's third-largest record label, was the third-largest contributor. WMG delivered improved revenue growth driven by increased market share and a better environment for ad-supported streaming. Price increases by leading distributors and new deals with some emerging platforms further fueled optimism that recent results are sustainable.

Largest Detractors

Omnicom (OMC), an international advertising holding company, was the largest detractor. OMC lagged due to concerns that clients could insource portions of their programmatic spending. Additionally, investors reacted poorly to the potential decline in overall advertising spending in the case of a recession.

Teleflex (TFX), a global developer and manufacturer of a diverse portfolio of single-use medical devices used to diagnose and treat patients, primarily in acute care settings, was the second-largest detractor. TFX was negatively impacted by sentiment shift within the Health Care sector associated with normalizing procedure growth and increasing pharmaceutical treatment of obesity.

Discover Financial Services (DFS), an owner and operator of a closed-loop branded credit card network targeting prime customers, was the third-largest detractor. An increase in charge-offs and delinquencies in credit card loans weighed on the stock. There were also concerns over a review of practices in their student loan servicing operations.

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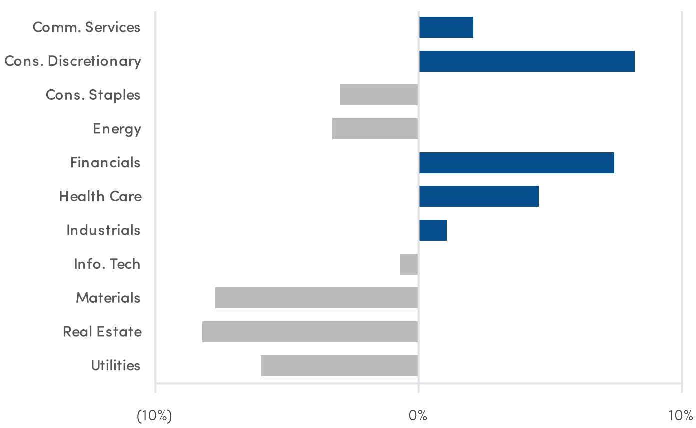
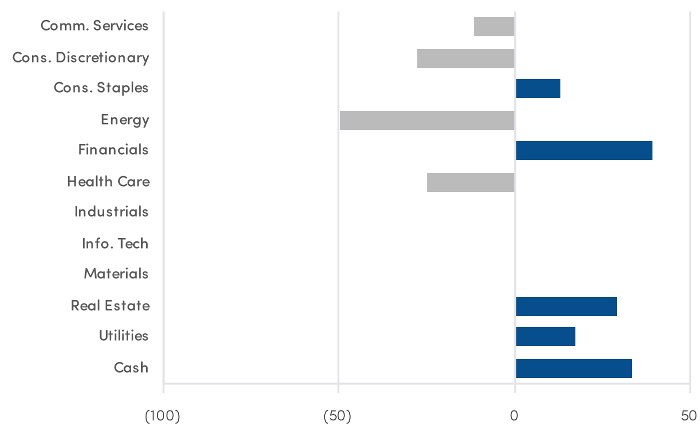
Sector Positioning

Sector allocation effect was additive during the third quarter. The portfolio's overweight to Financials, one of only two sectors with positive absolute performance within the benchmark, generated the largest contribution to relative results. Underweight positions in Real Estate and Utilities were also beneficial as bond proxy sectors faltered during the quarter. Conversely, the most significant headwind came courtesy of an underweight to Energy, which turned in a double-digit return driven by rising oil prices, easily surpassing the mostly negative returns posted by other benchmark sectors. The strategy's overweight to Consumer Discretionary and Health Care also weighed on portfolio performance.

Avg Wt Relative to RMV Index (%)



Allocation Effect (bps)



Source: FactSet

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Initiations

There were no initiations this quarter.

Eliminations

Fortrea (FTRE) was eliminated to make room for better opportunities.

Notable Stock Updates

Fortrea (FTRE), a leading provider of outsourced pharmaceutical late stage clinical trials, was spun-out of **Laboratory Corporation of America (LH)** during the quarter. The stock was eliminated to make room for better opportunities.

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Outlook

Although Cooke & Bieler's bottom-up process centers on individual company fundamentals, we remain keenly aware of the macroeconomic landscape and the hazards it may present. With the Fed having somewhat tamped inflation, the U.S. consumer displaying surprising resilience, and unemployment remaining low, the market's initial third quarter buoyancy was not entirely unfounded. That said, the recent spike in oil prices poses a clear headwind to disinflation, while the impending resumption of student loan payments could finally deplete consumers' pandemic savings buffer. Additionally, there is a growing sense that not only are policymakers' "higher for longer" talking points sincere with regards to interest rates, but many are expecting one remaining rate hike in 2023. With these developments, a soft landing scenario has become incrementally less likely. Investors have begun to rein in their expectations accordingly, but we are not yet convinced these expectations are aligned with the true risks. This disconnect strengthens the case for discerning stock selection, and we believe the style preferences displayed by markets during the quarter may prove enduring, which could benefit the portfolios going forward. Combining strong business quality, balance sheet strength, and good valuation – the intersection that Cooke & Bieler targets when choosing holdings – becomes more relevant during periods of economic turmoil.

Sources: Bloomberg, FactSet

Additional Cooke & Bieler Mid Cap Value Performance Disclosures