Cooke & Bieler

Q3 2021

Mid Cap Value Equity

Overview

Following a breakneck advance through the first half of the year, U.S. equity indices turned in mixed results for the third quarter. The market's tone shifted noticeably in September when investors faced increasing evidence that supply chain disruptions, rising input cost inflation, and labor shortages might negatively impact the near-term trajectory of the economic recovery. Presumably better equipped to handle such vagaries, large cap stocks generally outperformed smaller cap issues. Returns across styles, factors, and sectors were muddled. Growth outperformed value up the market cap spectrum while the opposite was true among small cap stocks. Notably, one consistent trend was Financials sector outperformance, largely driven by bank stocks.

Portfolio Performance & Developments

Cooke & Bieler's Mid Cap Value Strategy lagged the benchmark in the third quarter, posting a return of -1.85% gross of fees (-2.04% net of fees) versus -1.01% for the Russell Midcap® Value Index. Underperformance was attributable to a negative stock selection effect, which overwhelmed a modestly positive sector allocation effect. Weakness among the portfolio's Financials holdings accounted for the majority of the negative stock selection. More specifically, the strategy's skew towards insurance companies meaningfully detracted from relative performance as they generally did not participate in the success of the overall Financials sector. Consumer Discretionary and Industrials holdings also detracted from performance. Notably weak in these areas were American Eagle and Steelcase, which both highlighted near-term earnings challenges posed by supply chain disruptions when they reported before quarter end. Health Care stocks were a bright spot in the portfolio, led by Hill-Rom Holdings which received an attractive all-cash offer to be acquired by Baxter. Stock selection was also favorable in the Information Technology, Real Estate, and Consumer Staples sectors.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Hill-Rom	2.1	32.3	80
FirstCash	3.6	14.9	49
AerCap	2.8	12.9	34
Fidelity Nat'l. Financial	3.2	5.2	16
CBRE	1.0	13.6	14

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
American Eagle	2.2	-30.9	-75
Atmos Energy	2.1	-7.6	-17
Stanley Black & Decker	1.1	-14.1	-17
Woodward	2.2	-7.7	-17
Progressive	2.0	-7.9	-16

Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Mid Cap Value institutional portfolio's gross of fees return relative to the Russell Midcap® Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's Mid Cap Value clients. To obtain the calculation's methodology and a list showing every holding's contribution to the overall account's performance during the quarter, contact your client service representative or email your request to contact@cooke-bieler.com.

Largest Contributors

Hill-Rom (HRC), a provider of hospital beds and patient monitoring devices, was the largest contributor. Baxter International recently made an attractive all-cash offer to acquire the company.

FirstCash (FCFS), the largest pawn shop operator in North America and Mexico, was the second-largest contributor. After several quarters of weak results, FCFS saw rising loan volumes heading into the third quarter as government stimulus efforts subsided. Additionally, the company's retail merchandise is entirely locally sourced, immunizing it from the supply chain issues that have been plaguing other retailers.

AerCap (AER), the largest independent aircraft lessor, was the third-largest contributor. Global air travel entered the early stages of a recovery and investors began to appreciate the stability of the aircraft leasing business model. Additionally, the company's opportunistic acquisition of General Electric's aircraft leasing business highlighted management's astute capital management and the long-term potential for the business.

Cooke & Bieler

Q3 2021

Mid Cap Value Equity

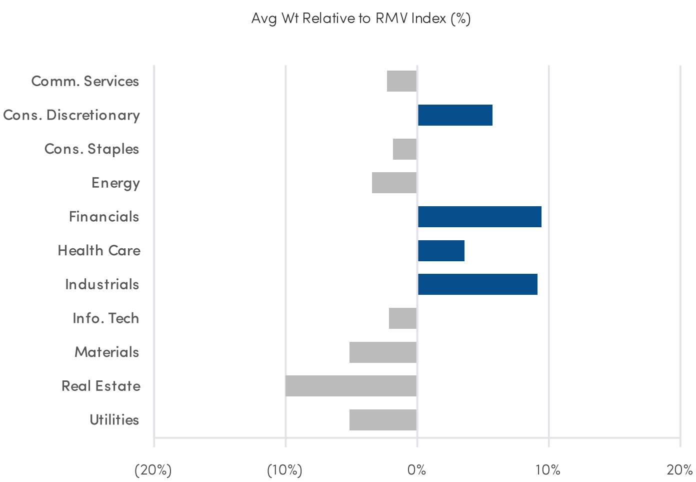
Largest Detractors

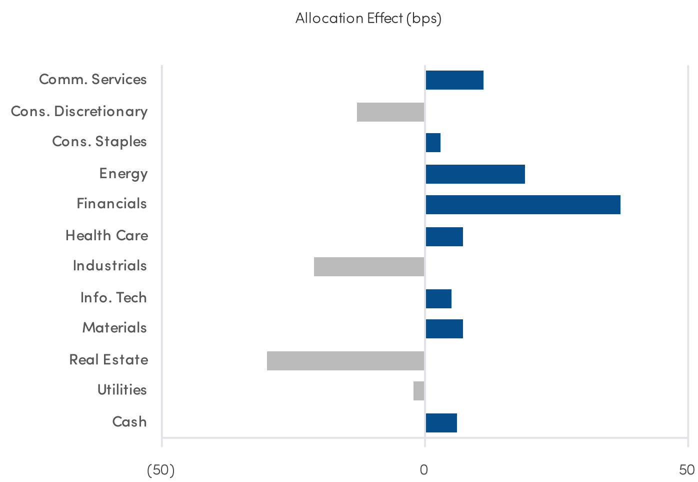
American Eagle Outfitters (AEO), a leading teen and young adult retailer operating through the American Eagle and Aerie brands, was the largest detractor. After a strong first half of the year, AEO disappointed investors by suggesting that margins would be restrained by increased shipping costs and supply chain challenges. These issues should prove temporary and should not detract from the long-term value AEO is building with its Aerie brand or the structural margin improvements they have made at their American Eagle concept.

Atmos Energy (ATO), one of the largest regulated gas utilities in North America, was the second-largest detractor. The higher interest rate environment caused investor sentiment to sour toward the Utilities sector in general. Natural gas utilities in particular are also facing concerns about future ESG-related headwinds.

Stanley Black & Decker (SWK), an industrial and household tool manufacturer, was the third-largest detractor. Supply chain bottlenecks and increased input product costs negatively affected the company's performance.

Sector Positioning





Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Mid Cap Value institutional portfolio's gross of fees sector return relative to the Russell Midcap® Value Index. Please see additional performance disclosures at the end of this document.

Sector allocation was additive in seven out of 11 sectors during the third quarter. The overweight to Financials was a particular positive standout, as it was the best performing sector in the Index. Also contributing to relative performance were underweight positions in Energy, Communication Services, and Materials. Offsetting much of this relative benefit was the strategy's significant underweight to Real Estate, which posted the second best return in the Index. The overweight to Industrials and Consumer Discretionary sectors, which seemed to be particularly exposed to supply chain issues, also detracted from results.

Mid Cap Value Equity

Initiations

Baxter International (BAX) develops, manufactures, and markets a diverse portfolio of lifesaving medical products, including intravenous (IV) solutions and medicines, IV pumps and sets, and peritoneal dialysis solutions and equipment. Revenue and margin pressures stemming from the pandemic should subside as the operating environment normalizes, clearing a path to sustained solid EPS growth. The proposed acquisition of Hill-Rom should be accretive to current earnings and future growth.

Dentsply Sirona (XRAY) is the largest manufacturer in the still fragmented global dental products and technologies market, an attractive and secularly growing market driven in part by aging demographics in developed markets and rising standards of living in emerging markets. XRAY's brands, scale, distribution, and stickiness with over 600,000 dental professional end users allow the company to earn attractive returns on capital, and relatively low capital requirements lead to consistent and substantial levels of free cash generation. Management has focused on simplifying the business, improving profitability, and investing organically and inorganically in attractively growing products such as clear aligners and implants to help spur improved organic growth.

PACCAR (PCAR) manufactures heavy and medium duty commercial vehicles sold under the Peterbilt, Kenworth, and DAF brands. PCAR also designs and manufactures diesel engines and other powertrain components for use in its own products and for sale to third parties. The company has managed to drive share gains in core markets while executing steady international expansion and building a strong aftermarket parts business, which offers a steady revenue stream and good growth potential. PCAR should also be able to participate in the growing electric vehicle market as it has already developed some electric vehicle products and capabilities. The stable business, growth opportunities, and history of strong returns to shareholders in the form of dividends make the stock an attractive holding.

Williams Companies (WMB) is a gas infrastructure company providing natural gas gathering, processing, and transmission services, as well as natural gas liquids fractionation, transportation, and storage services. WMB owns an interest in and operates over 30,000 miles of pipelines, including Transco, the nation's largest natural gas transmission pipeline. The company's interstate pipeline assets are a significant source of competitive advantage given the high levels of capital expenditure and permits required to create competing assets. The company generates adequate free cash flow to cover its high dividend yield and management is intently focused on improving overall return on capital.

Eliminations

Hill-Rom (HRC) reached our price target and was eliminated.

Synchrony Financial (SYF) was eliminated to make room for better opportunities.

Outlook

Having spent the last year pricing in an economic recovery propelled by re-opening and massive fiscal and monetary stimulus, markets are now grappling with the shape of the post-pandemic landscape. In particular, the question of whether current rates of inflation are transitory – caused by temporary supply chain disruptions – or if they reflect deeper structural issues, has increasingly dominated investors' thinking.

The prospect of persistent inflation raises questions markets have not faced in decades and, absent a ready playbook, the markets are likely to react strongly to suggestive data points and become even more volatile. Elevated valuations and Washington's characteristically chaotic approach to policy making further enhance the possibility of a bumpy ride. Faced with this uncertainty, our focus remains on using short-term volatility to acquire attractively-valued businesses that have the balance sheets to weather short-term supply disruptions and the competitive positions to prosper in a more difficult inflationary environment. While this approach does not yield results in every quarter, it has been key to the strategy's long-term success.

Sources: APX, Bloomberg, CNBC, CNN, FactSet, Nasdaq

Additional Cooke & Bieler Mid Cap Value Performance Disclosures