MID-CAP VALUE

MARKET COMMENTARY

The Russell Midcap Index declined -16.9% in the second quarter of 2022. The Russell Midcap Value Index declined -14.7% while the Russell Midcap Growth Index declined -21.1%. All eleven Russell Midcap GICS sectors declined in the quarter.

Several economic developments in the quarter sparked fears of a recession. Real GDP was -1.6% quarter-over-quarter (1Q), the war in Ukraine showed little signs of abating, the Consumer Price Index increased 8.6% year-over-year, and an increasingly hawkish FOMC raised the Fed Funds rate by 125 basis points via two hikes (from 0.5% to 1.75%). The Fed signaled further rate increases going forward to combat the highest inflation level in more than 40 years. The futures market implies that investors expect the Fed Funds rate to exceed 3% by year end with more rate hikes expected in 2023. Higher rates are generally bad for equities. It becomes more costly to borrow, increasing the cost of capital, which is the rate used to discount future cash flows. Higher rates impair long-duration equities disproportionately because most of the intrinsic value is derived from a terminal value estimate far into the future. In general, growth stocks are longer duration securities than value stocks. Unsurprisingly, value has outperformed growth in periods of elevated inflation and interest rates historically.

Value held up better than growth in the quarter. Energy and the least economically sensitive sectors—consumer staples and utilities—each declined less than 9% in the quarter. All other sectors declined -12% or more, with communication services (-26%), technology (-23%) and consumer discretionary (-20%) the worst performers. The portfolio is more heavily weighted to economically sensitive areas of the market, with energy, financials, and industrials being our largest sector weights relative to the Russell Midcap Value Index. The stocks we own in these sectors have good balance sheets, generate attractive free cash flow, and trade at large discounts to other parts of the market generally viewed as high quality businesses, e.g., consumer staples, though with superior growth prospects.

Despite value's recent outperformance, the valuation spread between growth and value remains wide because the spread at the period's outset was extreme. The Russell Midcap Value trades at 12x forward P/E (consensus FY1) compared to the Russell Midcap Growth at 18x. We believe these large spreads and the macroeconomic backdrop should continue to benefit value relative to growth, which should be a conducive environment for our investment approach.

ATTRIBUTION – 2Q22

The Hotchkis & Wiley Mid-Cap Value portfolio (gross and net of management fees) underperformed the Russell Midcap Value Index in the second quarter of 2022. Stock selection in energy was the leading detractor from relative performance during the quarter. Stock selection in communication services and consumer discretionary also detracted. The overweight in energy and stock selection in technology and financials contributed positively to performance. The largest positive contributors to relative performance in the quarter were First Citizens BancShares, Popular, Vistra Energy, NRG Energy, and Cenovus Energy; the largest detractors were Warner Bros. Discovery, The ODP Corp., Olin Corp., Adient, and Universal Health Services.

LARGEST NEW PURCHASES – 2Q22

Gap Inc. is a global apparel retailer selling four key brands: Old Navy, Gap, Banana Republic, and Athleta. The company operates as an omni-channel retailer, with ~40% of sales coming from digital platforms and the rest from brick-and-mortar locations. The collection of brands has ~3,400 stores, with just over 2,800 corporate owned stores and ~550 franchise locations. Over half of sales come from Old Navy, while less than 20% of revenue is generated from indoor malls. The company has been closing locations and exiting businesses as part of an effort to optimize the portfolio. We believe the portfolio is well positioned for recovery: Old Navy has limited competition at its price point, Athleta is growing rapidly, and Banana Republic is benefitting from a more casual return to work dress code. At 5.3x our view of normal earnings, we think the recent sell-off is overdone, and believe we are buying a collection of reasonably well-positioned brands for a very good price.

Olin Corp. is the largest global producer of chlor alkali chemicals and chlorine derivatives. Olin was incorporated in 1892 and is headquartered in Virginia. In a healthy GDP scenario, Olin's earnings should remain elevated, particularly with structural changes to chlorine pricing and recent cost-cutting efforts. Olin trades at a significant discount to our assessment of normal earnings, has a strong balance sheet, and the business is diversifying to our existing commodity exposure.

Stanley Black & Decker Inc. (SWK) is a leading manufacturer of consumer and professional hand tools and power tools, as well as fasteners and fittings for the automotive, industrial, infrastructure and oil & gas end-markets. SWK has significantly lagged the market since December 2019, as concerns about market share loss, interest rates, inflation and a consumer slowdown has hurt sentiment. We believe that market share loss concerns are overblown, as SWK has, in fact, maintained market share, and that SWK is less exposed to consumer spending than the market believes. In addition, SWK should be able to grow at an above GDP pace over the long term, due to its exposure to the faster growing corded and gas-powered equipment markets and should benefit from industry consolidation as large tools manufacturers take share from smaller ones. SWK has historically compounded earnings at an ~11% rate over the last 20 years, offers an above average dividend yield, and has performed well in previous recessions. SWK currently trades at ~10x our estimate of normal

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Composite performance is available at www.hwcm.com, located on the strategy's Performance tab. Returns discussed can differ from actual portfolio returns due to data differences, cash flows, trading, and other activity. Portfolio characteristics and attribution based on representative Mid-Cap Value portfolio. Certain client portfolio(s) may or may not hold the securities discussed due to each account's guideline restrictions, cash flow, tax and other relevant considerations. Performance attribution is an analysis of the portfolio's return relative to the index, is calculated using daily holdings information and does not reflect management fees and other transaction costs and expenses. For the portfolio's total performance attribution, interaction effect is combined with stock selection. Specific securities identified are the largest contributors (or detractors) to the portfolio's performance relative to the index. Other securities may have been the best and worst performers on an absolute basis.

The value discipline used in managing accounts in the Mid-Cap Value strategy may prevent or limit investment in major stocks in the Russell Midcap, Russell Midcap Value and Russell Midcap Growth and returns may not be correlated to the indexes. Quarterly characteristics and portfolio holdings are available at www.hwcm.com, located on the strategy's Portfolio and Literature tabs. For a list showing every holding's contribution to the overall account's performance and portfolio activity for a given time period, contact H&W at hotchkisandwiley@hwcm.com. Portfolio information is subject to the firm's portfolio holdings disclosure policy.

Equity securities may have greater risks and price volatility than U.S. Treasuries and bonds, where the price of these securities may decline due to various company, industry and market factors. Investing in small and medium-sized companies involves greater risks than those associated with investing in large company stocks, such as business risk, significant stock price fluctuations and illiquidity.

The "Largest New Purchases" section includes the three largest new security positions during the quarter/year based on the security's quarter/year-end weight adjusted for its relative return contribution; does not include any security received as a result of a corporate action. If fewer than three new security positions during the quarter/year, all new security positions are included. Securities identified do not represent all of the securities purchased or sold for advisory clients and are not indicative of current or future holdings or trading activity. H&W has no obligation to disclose purchases or sales of the securities. The largest new purchases are as of the publication date but may be sold and no longer held in the Mid-Cap Value strategy at any time, for any reason, without notice, subsequent to the publication date. The securities reflected herein are intended to be for illustrative purposes only and are not intended to be, and should not be construed as, investment recommendations or investment advice. Past performance of these securities, or any other investments, is not an indicator of future results. H&W's opinions regarding these securities are subject to change at any time, for any reason, without notice. No assurance is made that any securities identified, or all investment decisions by H&W were or will be profitable.

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Style Risk: A value-oriented investment approach involves the risk that value stocks may remain undervalued or may not appreciate in value as anticipated. Value stocks can perform differently from the market as a whole or from other types of stocks and may be out of favor with investors and underperform growth stocks for varying periods of time.

Market Disruption: The global coronavirus pandemic has caused disruption in the global economy and extreme fluctuations in global capital and financial markets. H&W is unable to predict the impact caused by coronavirus pandemic, which has the potential to negatively impact the firm's investment strategies and investment opportunities.

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Past performance is no guarantee of future results.