Diamond Hill Corporate Credit Strategy

As of September 30, 2020

All Composite returns are net of fees.

The Composite generated a 5.26% total return during the third quarter, compared to a 2.12% total return for the ICE BofA U.S. Corporate & High Yield Index. Year-to-date, the strategy generated a 4.19% total return compared to 5.64% total return for the Corporate & High Yield Index. For the trailing five years, the strategy generated an annualized total return of 7.61% compared to 6.15% for the Corporate & High Yield Index.

Unlike most corporate bond strategies, the Diamond Hill Corporate Credit strategy is not managed against any index. Instead, the strategy is managed against absolute objectives within a range of inflation plus 3% and 7% nominal, each measured over rolling five-year periods. Our goal is to generate a yield and total return within that range while minimizing the risk of downside volatility over longer time periods. Although the strategy's investable universe (and the Corporate & High Yield Index) includes both investment grade and high yield corporate bonds, since early 2010 the strategy has been largely focused on the high yield portion of the market to achieve these objectives. About 83% of the strategy was in high yield corporate bonds at the end of the third quarter.

The high yield portion of the U.S. corporate bond market, as represented by the ICE BofA U.S. High Yield Index, began the quarter with a yield-to-worst (YTW) of 6.85% and an option-adjusted spread (OAS) of 644 basis points (bps). After generating a 4.71% total return for the quarter, the High Yield Index ended the quarter with a 5.76% YTW and OAS of 541 bps. On a year-to-date basis, the strategy's 4.19% total return compares to -0.30% for the High Yield Index, 5.57% for the S&P 500 Index and -8.69% for the Russell 2000 Index.

TEAM

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From the March 23 bottom of the market for corporate bonds and stocks, the strategy has returned over 22%. Yet we are still finding good values in the high yield bond market. How can that be? Perhaps the most important development is that high yield companies have issued close to $280 billion of bonds in the last two quarters representing almost 20% of the $1.45 trillion value of the high yield market. Most of this cash has been used to refinance debt or to place cash on the balance sheet to ensure against adverse economic outcomes. So this issuance has materially improved the credit quality of the high yield market. Price is to some extent independent of value but when new issuance is so high, price actually has an important positive impact on value.

While new issue supply may begin to slow, we don't believe demand will be a limiting factor. U.S. high yield is, in our opinion, one of the safer places globally to generate a yield above inflation. As a result, investors who can't achieve their objectives with negative real – let alone negative nominal – yields may continue to find their way to U.S. high yield.

Another important development is the increase in value of the equity cushion that is subordinate to debt in the capital structure. As proxies for the increase in value of that equity cushion, since March 23, both the S&P 500 and the Russell 2000 have returned over 51%.

As a result of these developments, forecasts for high yield defaults have come down dramatically. In March, the starting point for default forecasts was the experience during the global financial crisis. But defaults have actually leveled out in the 7% range for the last four months, one-third to one-half of the peak default rate in 2009 depending on the data set. Now some forecasters are starting to conclude that defaults have peaked.

DIAMOND HILL CAPITAL MANAGEMENT

Policy makers – in the U.S., the Fed, Treasury and Congress – have played a huge role in the much-better-than-feared outcome to this point. In particular, the Fed, in partnership with Treasury, has $750 billion of buying power in the corporate bond market (both secondary market and new issues) but has only used about $13 billion. We believe that any sustained widening of credit spreads would be met with increased Fed buying making the sustained widening less likely.

Fiscal stimulus has also been a major factor in the performance of risk assets. While the near-term prospects are highly uncertain, looking out six months we believe there is a high probability of meaningful additional fiscal stimulus.

The strategy's YTW is typically somewhere in the range of our absolute objectives, although it was well below the low end of the range in late June 2014 and well above the high end of the range in early February 2016 and again at the beginning of the second quarter when the strategy's YTW was 8.02%. At the end of the third quarter, the strategy's YTW was 5.33% and the effective duration was 4.03.

As always, we are focused on delivering risk-adjusted returns over a complete market cycle by holding up better during down markets and capturing our fair share of the upside in strong markets. We also want to be in a strong position to take advantage of volatility and illiquidity in the corporate bond market. We expect near-term volatility due to the election, fiscal stimulus negotiations and the global pandemic. But we are confident that six months from now, much of the uncertainty surrounding these issues will be resolved and we remain positive on the prospects for the high yield asset class and the strategy.

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PERIOD & ANNUALIZED TOTAL RETURNS (%)

Inception Date: September 30, 2002

	SINCE INCEPTION	10-YR	5-YR	3-YR	1-YR	YTD	3Q20
CORPORATE CREDIT COMPOSITE							
Gross of Fees	7.67	7.04	8.09	6.89	7.21	4.54	5.38
Net of Fees	7.17	6.54	7.61	6.41	6.73	4.19	5.26
BENCHMARKS							
ICE BofA U.S. Corporate & High Yield Index	6.25	5.41	6.15	6.04	7.07	5.64	2.12
ICE BofA U.S. High Yield Index	8.36	6.28	6.61	3.83	2.30	-0.30	4.71

CALENDAR YEAR RETURNS (%)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
CORPORATE CREDIT COMPOSITE										
Gross of Fees	14.52	6.30	10.65	6.12	3.15	2.19	12.90	8.56	1.26	13.91
Net of Fees	13.96	5.78	10.11	5.60	2.64	1.72	12.40	8.07	0.81	13.41
BENCHMARKS										
ICE BofA U.S. Corporate & High Yield Index	10.76	6.80	11.37	0.34	6.43	-1.37	7.97	6.66	-2.21	14.28
ICE BofA U.S. High Yield Index	15.19	4.38	15.58	7.42	2.50	-4.64	17.49	7.48	-2.26	14.41

Analytics provided by The Yield Book® Software. Diamond Hill Capital Management Inc. (DHCM) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS Standards. Diamond Hill has been independently verified for the period 5/31/00 – 6/30/20. Diamond Hill's current verification firm is ACA Compliance Group. The verification report(s) is/are available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation. Diamond Hill is a registered investment adviser and wholly owned subsidiary of Diamond Hill Investment Group, Inc.; registration does not imply a certain level of skill or training. Diamond Hill provides investment management services to individuals and institutional investors through mutual funds and separate accounts. A complete list and description of all composites and policies for valuing portfolios, calculating and reporting returns, and preparing compliant presentations are available upon request. The Corporate Credit Composite is comprised of discretionary fee paying non-wrap accounts with a market value over $10M managed according to the firm's Corporate Credit fixed income strategy. The strategy's investment objective is to provide an attractive cash distribution and total return greater than the current rate of inflation, while minimizing the risk of a current loss of capital over a five-year time horizon. The strategy generally invests in investment grade and below-investment grade (high yield) corporate bonds and will typically maintain an effective duration less than five. The Composite results reflect the reinvestment of dividends, capital gains, and other earnings when appropriate. Composite returns and benchmark returns are presented gross of withholding taxes on dividends, interest income and capital gains. Returns are calculated using U.S. Dollars. Net returns are calculated by reducing the gross returns by either the actual client fee paid or the highest stated fee in the Composite fee schedule, depending on the type of client and account, and are reduced by estimated accrued performance based fees where applicable. Only transaction costs are deducted from gross of fees returns. The ICE BofA U.S. Corporate & High Yield Index is the primary benchmark. This index is comprised of U.S. dollar denominated investment grade and below investment grade corporate debt publicly issued in the U.S. domestic market. The ICE BofA U.S. High Yield Index is shown as additional information. This index is comprised of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market. Ratings are based on an average of Moody's, S&P and Fitch. Our selection process may lead to portfolios that differ markedly from the benchmarks presented. Returns may be more volatile than, and/or may not be correlated to these indices, which are for comparative purposes only. The Firm's standard fee schedule for Corporate Credit separate accounts is as follows: First $50,000,000 = 0.55%; Over $50,000,000 = 0.45%. The dispersion measure is the asset weighted standard deviation of the annual portfolio returns. Only portfolios represented in the Composite for the entire year are included in the calculation. The calculation is not performed if the Composite contains 5 or fewer accounts for the full year. No alteration of composites as presented here has occurred because of changes in personnel at any time. **Past performance is not a guarantee of future results.** It should not be assumed that an investment in the securities identified was or will be profitable. The holdings identified do not represent all of the securities purchased, sold, or recommended for the adviser's clients. To obtain the contribution calculation methodology and a complete list of every holding's contribution to the overall portfolio's performance during the measurement period, please contact 855.255.8955 or info@diamond-hill.com. GIPS is a trademark of CFA Institute. CFA Institute has not been involved in the preparation or review of this report/advertisement. The index data referenced herein is the property of ICE Data Indices, LLC, its affiliates ("ICE Data") and/or its third party suppliers and has been licensed for use by Diamond Hill Capital Management, Inc. ICE Data and its third party suppliers accept no liability in connection with its use. See diamond-hill.com/disclosures for a full copy of the disclaimer.

AS OF YEAR-END	DHCM	CORPORATE CREDIT COMPOSITE			3-YR ANNUALIZED STANDARD DEVIATION (GROSS OF FEES)		
	Assets Under Management	Number of Accounts	Assets Under Management	Dispersion (Gross of Fees)	Corporate Credit Composite	ICE BofA U.S. Corporate & High Yield Index	ICE BofA U.S. High Yield Index
2019	$23.4B	5 or fewer	$1.1B	NA [1]	2.69%	3.22%	4.13%
2018	19.1B	5 or fewer	743.4M	NA [1]	3.35	3.43	4.64
2017	22.3B	5 or fewer	652.4M	NA [1]	3.78	3.63	5.60
2016	19.4B	5 or fewer	533.5M	NA [1]	3.96	3.93	6.03
2015	16.8B	5 or fewer	333.5M	NA [1]	2.91	3.81	5.27
2014	15.7B	5 or fewer	220.0M	NA [1]	2.37	3.77	4.44
2013	12.2B	5 or fewer	186.7M	NA [1]	3.31	4.33	6.42
2012	9.4B	5 or fewer	178.4M	NA [1]	3.80	4.00	7.03
2011	8.7B	5 or fewer	146.0M	NA [1]	7.10	5.71	11.00
2010	8.6B	5 or fewer	145.8M	NA [1]	NA [2]	NA [2]	NA [2]

[1] NA = Not Applicable

[2] Statistics are not presented because 36 monthly returns are not available.

This composite was created in April 2015.

Global Investment Performance Standards