

Large Cap Strategy

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DIAMOND HILL
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Quarterly Snapshot

Performance

The Strategy returned 3.18% (net of fees) compared to a 2.61% return for the Russell 1000 Value Index.

Key Drivers

Stock selection in information technology, our underweight in utilities and our overweight in energy were the three largest contributors to relative performance. Stock selection in industrials, health care and consumer staples were the largest detractors from performance.

Summary

We believe above-average equity market valuations are likely to lead to below-average returns over the next five years. However, we continue to find attractive opportunities on a bottom-up basis and are confident we can achieve better-than-market returns over the next five years through active portfolio management.

Market and portfolio review

Information technology (+13%) was again among the best performing sectors within the Russell 1000 Value Index; however, during the quarter we saw a reversal in areas of the sector that have either led or lagged. Software and other legacy technology companies outperformed in 3Q26. Although many were recently removed from the value index in June's Russell reconstitution, several of the AI-spending beneficiaries that contributed to index returns in recent quarters were weak. Energy (+16%) was the best-performing sector as a resolution to the war in Iran remains elusive. The communication services (+10%) and health care (+9%) sectors also performed well, while the sharp rise in interest rates weighed on utilities (-12%), industrials (-6%) and real estate (-6%).

After assuming responsibility on July 1, the new portfolio management team repositioned the portfolio to reflect their highest conviction ideas, which included nine new and 14 eliminated positions. The most notable change was increased exposure to several companies we believe are well positioned to be long-term beneficiaries of AI, but importantly, each also has a high quality and dominant core business. To help fund these additions, we eliminated or reduced several positions whose fundamentals have been uninspiring, which included a significant reduction in consumer staples exposure. Other changes included modest repositioning in financials, where we reduced exposure to insurance and added to banks, and in energy, where we reduced exposure to natural gas to gain more oil exposure.

Unlike recent quarters when the information technology sector was the largest detractor from the portfolio's relative performance, it was the largest contributor to performance in 3Q26. Our software holdings, including Salesforce and Microsoft, rose significantly as fundamentals remain strong and as investor sentiment seems to be modestly improving. Valuations remain attractive, in our view.

A new position in Meta Platforms was a contributor after releasing its AI agent, Muse, which has gained rapid adoption. Counting nearly half the world's population as users of its platforms, Meta is in an enviable position to roll out such products to its vast user base. With the sharp rise in interest rates in 3Q26, our holdings with rate-sensitive housing exposure were weak, including Carrier Global, Builders FirstSource, NVR, Martin Marietta Materials and Ferguson. In financials, Aon was a notable detractor after announcing a large, fairly expensive deal to expand its middle markets business.

Key contributors

- Shares of **Microsoft** rose after the company reported strong Azure results that included a growth reacceleration in quarterly results and guidance. Microsoft remains very well positioned to implement AI into its current offerings while also adding enormous AI computing capacity to lease to customers on attractive economic terms.

- Customer relationship management software provider **Salesforce** outperformed on strong 2027 guidance, creating a solid set-up for reaccelerating revenue growth. Additionally, revenue for the company's generative AI offering is growing, and the company's headless initiatives stand to further accelerate revenue growth.
- Shares of health care tools and diagnostics company **Thermo Fisher Scientific** outperformed following strong second quarter results and improving customer activity across key life sciences end markets, reinforcing confidence in continued demand recovery.

Key detractors

- Insurance broker **Aon** underperformed during the quarter amid concerns that the company overpaid for its acquisition of middle-market broker, USI. Investors also questioned whether Aon can accelerate organic growth in the acquired business moving forward.
- **Carrier Global**, a provider of residential and commercial HVAC, underperformed following mixed results after better-than-expected revenue growth was offset by weaker margins amid tariffs and inflation. Shares were also pressured by concerns surrounding the sustainability of data center spending and higher interest rates delaying a residential HVAC recovery. Despite near-term headwinds, we believe Carrier is well positioned to gain market share and improve margins long term.
- Shares of building materials and services supplier **Builders FirstSource** underperformed amid expectations for declining revenue. The Federal Reserve's first rate hike since July 2023 pushed interest rates higher, which weighed on the outlook for residential construction.

New positions

- **Taiwan Semiconductor Manufacturing** is the world's largest semiconductor foundry, manufacturing advanced chips for leading technology companies. We are attracted to the company's direct exposure to growing AI-computing demand, supported by its leadership in advanced chip manufacturing and strong profitability.
- We initiated a position in **JPMorgan Chase**, a global financial services firm, as we believe its scale enables continued technology investment that should improve efficiency over time. While some of these gains will be reinvested to support revenue growth, we expect improved efficiency to help contain expense growth and drive both positive operating leverage and stronger returns.

- We added energy company **Chevron** to the portfolio given its leverage to higher oil prices and refining margins, which benefited from renewed hostilities in the Middle East and continued tightness in the refinery complex. We also viewed the company's plans to increase production in Venezuela following the Trump administration's oil agreement as a potential source of additional growth.
- We initiated a position in a global technology company **Alphabet** as we believe AI is strengthening its core search and advertising business as well as several other products. Additionally, Google Cloud has emerged as a leading AI-infrastructure platform, supporting attractive and profitable revenue growth.
- **Meta Platforms** is the world's largest social media company and operates several applications, including Facebook, Instagram, Messenger, WhatsApp and Threads, serving more than 3.5 billion daily active users. We initiated a position as we believe the market is underappreciating the company's accelerating core advertising business and broad distribution advantages, creating an attractive entry point from a valuation perspective.
- **Stryker** is a medical technology company providing surgical equipment, instruments and implants across orthopedic and neurovascular markets. The company's broad product portfolio, consistent innovation and strong commercial execution, position Stryker to continue gaining market share and delivering above-market growth.
- We initiated a position in research and advisory firm **Gartner** as concerns around slowing revenue growth and potential disruption from AI have created an opportunity to invest at an attractive valuation. While AI introduces both risks and opportunities, we believe the market is underestimating the value of a Gartner license and the company's intermediate-term growth trajectory.
- We initiated a position in **Transocean**, a leading offshore drilling contractor, as constrained industry supply and rising demand create a favorable backdrop for offshore drilling. We believe the company is well-positioned to benefit as energy companies seek to replenish reserves and countries prioritize domestically controlled oil supplies. Its pending merger with Valaris further strengthens its position and improves its balance sheet.
- **Ameren**, a regulated electric and gas utility, was added to the portfolio given its combination of steady growth, a strong balance sheet and supportive regulatory environment. We believe its attractive rate base growth outlook should also support long-term growth.

Eliminated positions

Shares of the following companies were sold to allocate funds to more attractive opportunities.

- Accenture
- Builders FirstSource
- CarMax
- Colgate-Palmolive
- Cooper Companies
- EQT
- FedEx Freight
- General Mills
- Humana
- Kimberly-Clark
- MetLife
- Pfizer
- SBA Communications
- Texas Instruments

Period and Annualized Total Returns (%)	Since Inception (30 Jun 2001)	20Y	15Y	10Y	5Y	3Y	1Y	YTD	3Q26
Gross of Fees	9.62	9.31	12.47	10.47	6.45	11.80	6.15	4.63	3.33
Net of Fees	8.88	8.61	11.78	9.80	5.81	11.13	5.52	4.16	3.18
Russell 1000 Value Index	8.43	8.60	12.98	11.43	11.92	20.07	23.81	19.27	2.61
Russell 1000 Index	9.62	11.16	15.50	15.04	13.01	22.48	15.01	12.30	1.80

Calendar Year Returns (%)	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Gross of Fees	3.60	13.35	37.79	11.58	-0.17	15.27	21.10	-8.81	32.96	9.99	26.50	-12.83	14.37	12.74	6.19
Net of Fees	2.87	12.61	36.89	10.86	-0.82	14.57	20.37	-9.36	32.16	9.33	25.74	-13.35	13.68	12.06	5.55
Russell 1000 Value Index	0.39	17.51	32.53	13.45	-3.83	17.34	13.66	-8.27	26.54	2.80	25.16	-7.54	11.46	14.37	15.91
Russell 1000 Index	1.50	16.42	33.11	13.24	0.92	12.05	21.69	-4.78	31.43	20.96	26.45	-19.13	26.53	24.51	17.37

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