Long-Short Strategy

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DIAMOND HILL
A First Eagle Investments Company

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Quarterly Snapshot

Performance

The Strategy declined 4.72% (net of fees) compared to a 4.18% decline for the Russell 1000 Index and a 2.15% decline for the 60/40 Blended Benchmark.

Key Drivers

On the long side, stock selection in industrials and consumer staples was the most notable detractor from relative performance. Stock selection in consumer discretionary, our underweight to information technology and our overweight to energy were the most notable contributors. Our short positions in industrials and consumer discretionary detracted the most from relative performance, while our information technology shorts contributed the most.

Summary

We believe above-average equity market valuations are likely to lead to long-term returns below historical averages, but we remain focused on finding individual businesses that are mispriced. If we are in a lower return equity market, alpha generation in each of the long and short books is even more important to achieving satisfactory returns over time.

Market and portfolio review

Equity market volatility picked up in Q1 due in large part to the ongoing war in Iran. After starting the year modestly positive through February, the Russell 1000 Index ended Q1 down 4.2%. Unsurprisingly, energy (+38%) was by far the best-performing sector, with oil prices rising sharply as global supplies were impacted by the closure of the Strait of Hormuz. Materials (+10%) and utilities (+8%) also saw strong outperformance in Q1, while financials (-10%), consumer discretionary (-9%) and information technology (-9%) were the worst-performing sectors.

The portfolio modestly trailed the long-only benchmark in Q1. Our long positions trailed the Russell 1000 Index by 200 basis points (bps), and our short positions were just over 200 bps ahead, leading to an unfavorable long-short spread (the performance of our long positions relative to the performance of our short positions) of 420 bps. Our long positions in software businesses, including Microsoft, Salesforce and Adobe, were among the most notable detractors in the quarter. While artificial intelligence (AI) poses legitimate risks of varying degrees to these businesses, the fundamentals of each remain quite good and valuations imply a scenario that is too pessimistic, in our view.

Net exposure of 58% remains modestly below our 60% long-term average, with long exposure ending the quarter around 90% and short exposure around 32%. This leaves gross exposure at 122%, a level we would like to modestly increase over time. However, we will be disciplined in doing so. We continue to find compelling long opportunities, but with elevated valuations across the market, we want to be very confident that the stocks we own will grow more valuable over time. We do not want to assume excessive risk when we are not being compensated to do so. It continues to be a fruitful environment to find attractive short opportunities as elevated expectations across a range of stocks have pushed valuations higher.

Key contributors

Long portfolio

- Exploration and production companies **Chevron** and **Diamondback Energy** saw shares rise as the sharp increase in oil prices drove a broad rally across US-based oil producers. As geopolitical tensions in the Middle East tightened the supply outlook, investors increasingly rewarded US producers for their leverage to higher commodity prices, potential for outsized cash generation and capacity for strong capital returns.
- **Taiwan Semiconductor** is the world's largest dedicated chip foundry, holding approximately 70% market share and advanced manufacturing capabilities. Shares outperformed following strong demand for its services, driven by artificial intelligence and high-performance computing chips.

Short portfolio

- All key contributors were long positions.

Key detractors

Long portfolio

- Shares of **Microsoft** declined amid concerns over slowing Azure revenue growth and capacity constraints. We believe the company's evolving relationship with OpenAI, along with near-term challenges in balancing internal and external demand for limited computing resources, has shifted focus from its long-term competitive advantages and growth in intrinsic value.

- Shares of **Salesforce** declined amid concerns around generative AI competition. Despite a more prolonged slowdown than initially anticipated, growth appears poised to reaccelerate in 2026, and if management's longer-term guidance proves accurate, revenue growth and profitability should trend higher over time.

- New holding **BellRing Brands**, a consumer nutrition company focused on ready-to-drink protein shakes including Premier Protein, saw shares decline following retailer inventory adjustments and increased promotional activity from newer competitors, which weighed on sales and margins. While results reflected higher input costs and more cautious guidance, underlying demand has remained resilient. We believe the recent weakness reflects timing and competitive dynamics rather than a structural change, and the company remains well-positioned within a growing category.

Short portfolio

- All key contributors were long positions.

New positions

Long Portfolio

- 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 subscription and the company's intermediate-term growth trajectory.

Short portfolio

- Global shipping company **Frontline** specializes in seaborne crude oil transportation. The crude oil tanker industry has benefited from a combination of supply and demand tailwinds that have driven spot rates to elevated levels. We expect these tailwinds to fade as vessel flows resume through the Strait of Hormuz, a wave of very large crude carrier supply comes to market and fleet dynamics remain oversupplied. As a highly cyclical, fixed-cost shipping business, we believe these dynamics will pressure earnings power from current levels over time.

- **NewMarket** is a specialty chemicals company focused on lubricant additives. The company has benefited from one-time tailwinds in recent years, which drove gross profit per ton meaningfully above longer-term averages. However, these tailwinds are now unwinding amid renewed competition, increasing Chinese supply and demand headwinds. Today, shares trade at an elevated valuation despite these pressures, which we believe will weigh on results over time.

- **Akamai Technologies** has pivoted from its legacy content delivery network business toward security and cloud services. Its newer growth engine, cloud infrastructure services, remains relatively small, capital-intensive, and is increasingly reliant on pricing rather than differentiated capabilities. As growth has stabilized, we believe intensifying competition, uncertain margin sustainability and limited differentiation in its cloud offering will pressure results over time.

- We initiated a short position in **Boot Barn** as we believe the company's future revenue growth will be challenged by its reliance on denim to drive comparable sales and worsening new store economics.

Eliminated positions

Long portfolio

- We exited our position in software company **Ciena** as shares approached our estimate of intrinsic value amid optimism around demand for optical equipment in AI data center buildouts.

- Shares of global investment firm **KKR** were sold in favor of more attractive opportunities.

Short portfolio

- We exited our short position in cloud-based project management software **Asana**, REIT **Vornado Realty Trust** and restaurant brand **Shake Shack** as shares fell below our estimate of intrinsic value.

- We exited our position in medical device manufacturer **Penumbra** after the company announced its acquisition by Boston Scientific.

Period and Annualized Total Returns (%)

	Since Inception (30 Jun 2000)	20Y	15Y	10Y	5Y	3Y	1Y	YTD	1Q26
Gross of Fees	8.63	7.57	9.08	9.21	8.91	13.63	12.04	-4.48	-4.48
Net of Fees	7.54	6.50	7.99	8.12	7.82	12.49	10.92	-4.72	-4.72
Russell 1000 Index	8.07	10.46	13.09	13.97	11.34	18.14	17.74	-4.18	-4.18
60%/40% Blended Index	5.86	7.17	8.59	9.45	8.41	12.84	12.24	-2.15	-2.15
Russell 1000 Value Index	8.02	8.12	10.47	10.58	9.43	14.31	15.87	2.10	2.10

Calendar Year Returns (%)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Gross of Fees	4.84	10.30	25.03	9.24	0.18	12.34	7.85	-5.46	25.15	1.41	21.40	-6.92	14.27	12.09	21.07
Net of Fees	3.90	9.30	23.91	8.26	-0.72	11.33	6.88	-6.31	24.02	0.50	20.30	-7.75	13.25	10.97	19.86
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
60%/40% Blended Index	1.22	9.75	18.93	7.86	0.75	7.33	12.92	-1.92	19.15	13.30	15.35	-10.86	17.82	16.63	12.12
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

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