

DIAMOND HILL

INVESTED IN THE LONG RUN

Large Cap Fund

(closed to most new investors)

As of 30 Sep 2022

Market Commentary

US stocks closed the quarter down -4.5% (as measured by the Russell 3000 Index), bringing year-to-date losses to -24% and leaving stocks on track for their worst year since the 2008 financial crisis. While hope springs eternal for easing pricing pressures, latest data indicated inflation remained high at 8.3% in August (though a small decline from the July reading).

The current market environment is interesting as it has evolved from the acceleration in inflation, which concerned us starting back in 2019. The pandemic relieved a near-term trend in rising prices, but the subsequent economic recovery served to accelerate cyclical inflationary pressures. The response by the Federal Reserve was, at first, quite timid but has since become aggressive – too aggressive in our opinion. Most leading indicators of inflation, except wage inflation, are pointing to a meaningful decline in inflationary pressures. However, the Federal Reserve remains determined to continue raising interest rates, presumably until reported inflation data is more in line with its long-term targets. Since most inflation data are lagging indicators and Fed tightening impacts the economy with a meaningful delay, we run the risk of a significant economic slowdown caused by an overly restrictive central bank.

As we reflect on this tightening cycle and what it means for investors, we are struck by the relative strength of US financial institutions, particularly in comparison to past tightening cycles. There have been no major financial stresses or calamities. That said, we are concerned about international stresses as the incredible strength of the dollar combined with rising European energy costs may cause meaningful dislocations overseas. Perhaps economic pressures abroad will eventually cause the Fed to relax its strict approach. Fortunately, the current lack of stress in the US reflects the strengthened balance sheets of American financial institutions and the improved asset quality

Team

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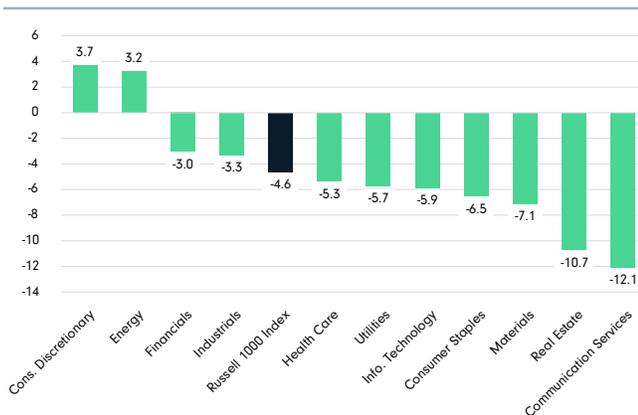
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Portfolio Specialist

compared to past cycles. We believe this should alleviate the severity of any economic slowdown, but paradoxically it may make it more difficult to quickly slow the economy, assuming that is the Fed's goal.

Finally, we think it is important to emphasize that the magnitude of the recent market selloff has historically been associated with meaningful investment opportunities for long-term investors. To better enable us to understand the long-term opportunity we looked at historical data since 1960. Over the prior 62 years there have been 17 selloffs of 19% or more. The data shows that purchasing the market after a 19% decline provides five-year annual returns approximately 200 basis points on average better than the historical average. This historical data is reassuring for investors maintaining a long-term perspective.

In summary, the market selloff has been painful, but at this point, we do not believe the current environment justifies another significant selloff. The financial system is strong, and corporate earnings, while under pressure, should prove more resilient than anticipated. Our expectation is that five years from now we will look back at this period and realize it was a great opportunity for long-term investors – that is why we consistently focus on a five-year time horizon. A short-term perspective too often causes investors to focus only on risk during times of market volatility. However, a five-year focus allows us to see the opportunities available, which have only multiplied with the decline in prices.

3Q22 Russell 1000 Index Sector Returns (%)



Source: FactSet, as of 30 Sep 2022.

Performance Discussion

Our portfolio trailed the Russell 1000 Index this quarter due in large part to the underperformance of our holdings in the technology and consumer discretionary sectors. Partially offsetting those results was positive stock selection in energy, consumer staples and materials.

On an individual holdings basis, top contributors to return included oil and gas producer ConocoPhillips and global technology company Nasdaq.

The rising price of both oil and natural gas has allowed ConocoPhillips to continue reporting strong earnings and cash flow growth even as the economic outlook becomes more uncertain. We continue to believe the company is an outstanding operator with a strong balance sheet and assets concentrated in well understood jurisdictions. While supply chain tightness has driven input prices higher within the industry, ConocoPhillips has kept its production and capex guidance steady for the full year as its longer-term service contracts help it push costs out into the future as compared to smaller competitors.

Geopolitical and macro-economic uncertainty, coupled with seasonality, resulted in a more challenging trading backdrop for Nasdaq this quarter. The company continues to execute well against the dynamic of a tougher market backdrop and the business remains resilient with good defensive attributes. Capital allocation priorities to strategic initiatives and shareholder returns remain positives. Long term, the market technology segment should drive growth as Nasdaq remains focused on strategic secular growth in areas such as: anti-financial crime, ESG, indexes and

investment analytics. The company continues to allocate capital to support these opportunities as a technology and analytics provider (increasingly as a SaaS-enabled technology provider).

Other top contributors in Q3 included agricultural equipment manufacturer Deere & Company, health care facilities operator HCA Healthcare and global online retailer Amazon. Deere has benefited as underlying demand for farm equipment remains healthy with strong commodity pricing and used equipment values providing support to farmer balance sheets. HCA outperformed low expectations when the company reported Q2 earnings with commentary that some of its cost pressures were easing. Amazon reported better-than-expected Q2 results, driven by a step-up in retail consumer demand, solid progress on remedying cost pressures (related to over investment) and strong performance in its web services business.

Our weakest performer in Q3 was apparel and footwear company VF Corporation. Consumer spending concerns weighed on the market's sentiment toward companies selling more discretionary goods. Additionally, management lowered guidance primarily due to weaker sales for its Vans brand, higher-than-expected industry discounting, and macroeconomic uncertainty. The remainder of the portfolio is performing well, as evidenced by solid refreshed long-term financial targets.

Also among our bottom contributors were health care products manufacturer Abbott Labs, global pharmaceutical company Pfizer, media and technology giant Alphabet, and insurance company American International Group (AIG).

Abbott has been working through a recall of its infant formula brand Similac in the US, which has continued to pressure its share price. Although the recall will impact near-term revenues, we are not concerned about any long-term impacts. We remain optimistic about the company given it is one of the highest quality names in health care, in our view, with a talented management team that makes smart capital allocation decisions. Abbott also has leading health care and consumer franchises with a particularly strong competitive position in its medical device business. The company continues to launch innovative products in key strategic areas (such as diabetes, structural heart, and diagnostics), which should help drive not only revenue growth but margin expansion.

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Shares of Alphabet underperformed on concerns of a weakening macroeconomic environment. The company also reported weaker-than-expected earnings and revenue for Q2 2022. Longer-term, we expect Google's search engine advertising, YouTube advertising and other initiatives to continue driving revenue growth and attractive margins.

Although Pfizer continues to report strong performance of its core drugs, sales of its COVID vaccine and treatment have likely peaked and sales are expected to decline going forward. We remain optimistic about the company long term as we believe management is taking the company in the right direction, focusing R&D, and making strategic acquisitions with profits generated from COVID vaccine sales.

AIG reported strong Q2 earnings, but volatile capital markets led to delays in the IPO of the company's life and retirement business and concerns about the quality of the company's investment portfolio. We continue to believe AIG has one of the best management teams in the industry, and they've been executing well on turning the business around and improving underwriting and expense control.

Portfolio Activity

Throughout 2022, our goal has been to continue taking advantage of the market selloff by focusing on areas of opportunity created by mispriced securities. At first, we recognized an opportunity in a few secular growth companies (Amazon, Alphabet, Microsoft) whose valuations declined due to rising interest rates. Then we focused on industrial monopolies (Martin Marietta Materials, Union Pacific, Waste Management) whose shares sold off meaningfully even though their long-term competitive positions made them resilient in the face of a potential economic slowdown. More recently, we increased our health care exposure (HCA Healthcare, Stryker) as this economically resilient sector sold off even though the fading pandemic was helping drive a secular improvement in earnings growth.

Stryker was the only new addition to the portfolio in Q3. It is one of the largest medical device manufacturers with a track record of consistently outgrowing its end markets and competitors. Stryker has a highly performance driven culture with a decentralized operating model that results in strong incentive alignment within the company. We believe the management team has executed well, making small but meaningful decisions that have positioned the firm well among competitors. Management operates with a market

share gain mentality and strives to be a category leader in the market they are in. Stryker also benefits from its broad portfolio of surgical tools, small and large cap hospital equipment, waste management products, etc., which enables it to address all the needs of a hospital operating room and be a one-stop shop for health care facilities. This is particularly appealing to hospitals, and it positions Stryker to be the supplier of all operating room equipment versus a single product, thus enabling the company to gain market share.

As we examine the market today, we are starting to become intrigued with economically cyclical areas of the market where company valuations have become depressed due to expectations of a near-term economic slowdown while the long-term competitive positions remain intact. These opportunities may be expressed by purchasing new positions in the portfolio or by increasing the position sizes of our current holdings that are cyclical companies. These companies are becoming especially attractive due to the serious price declines their stocks have experienced, and we think this area of the market is providing a great opportunity for long-term investors.

During the third quarter, we eliminated positions that have been the most disappointing to us from a fundamental perspective to make room for more attractive ideas. This quarter, that included Mondelez International, Meta Platforms, Hanesbrands and Cognizant Technology Solutions.

Market Outlook

As the US emerged from the pandemic, a sharp economic rebound, along with unprecedented fiscal and monetary stimulus, an uptick in wage growth and instances of supply/demand tightness, drove inflation to levels not seen in decades. In response, the Federal Reserve has aggressively tightened monetary policy and remains vocal about its commitment to rein in inflation, even if it must accept some economic pain to do so.

While the Federal Reserve continues to tighten monetary policy, a moderation of inflation, along with the sell-off in financial markets, rising mortgage rates and other factors that may slow broader demand could cause the Fed to act less aggressively. We've already seen a moderation in real GDP since its peak in Q4 2021. And while corporate earnings have been rising, a near-term economic slowdown and other factors like a strong US dollar could put pressure on corporate earnings going forward.

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This year's decline in equity markets has brought valuations back around historical averages and has created investment opportunities for valuation-disciplined investors in the process. Our primary focus is always on achieving value-added results for our existing clients, and we believe we can achieve better-than-market returns over the next five years through active portfolio management.

Period and Annualized Total Returns (%)	Since Inception (29 Jun 2001)	20Y	15Y	10Y	5Y	3Y	1Y	YTD	3Q22	Expense Ratio (%)
Class I (DHLRX)	8.13	10.34	7.21	10.32	6.19	4.93	-14.71	-21.97	-5.27	0.67
Russell 1000 Index	7.40	9.97	8.03	11.60	9.00	7.95	-17.22	-24.59	-4.61	—
Russell 1000 Value Index	6.61	8.67	5.71	9.17	5.29	4.36	-11.36	-17.75	-5.62	—

[Click here](#) for holdings as of 30 September 2022.

Risk disclosure: Overall equity market risks may affect the portfolio's value.

The views expressed are those of Diamond Hill as of 30 September 2022 and are subject to change without notice. These opinions are not intended to be a forecast of future events, a guarantee of future results or investment advice. Investing involves risk, including the possible loss of principal.

Past performance is not indicative of future results. Investment returns and principal values will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. The Fund's current performance may be lower or higher than the performance quoted. For current to most recent month-end performance, visit diamond-hill.com.

Performance assumes reinvestment of all distributions. Returns for periods less than one year are not annualized. Class I shares include Investor share performance achieved prior to the creation of Class I shares.

Fund holdings subject to change without notice.

Index data source: London Stock Exchange Group PLC. See diamond-hill.com/disclosures for a full copy of the disclaimer.

Securities referenced may not be representative of all portfolio holdings. Contribution to return is not indicative of whether an investment was or will be profitable. To obtain contribution calculation methodology and a complete list of every holding's contribution to return during the period, contact 855.255.8955 or info@diamond-hill.com.

Carefully consider the Fund's investment objectives, risks and expenses. This and other important information are contained in the Fund's prospectus and summary prospectus, which are available at diamond-hill.com or calling 888.226.5595. Read carefully before investing. The Diamond Hill Funds are distributed by Foreside Financial Services, LLC (Member FINRA). Diamond Hill Capital Management, Inc., a registered investment adviser, serves as Investment Adviser to the Diamond Hill Funds and is paid a fee for its services. Not FDIC insured | No bank guarantee | May lose value