Westwood Quality Value Fund (WHGLX)

Commentary

1Q 2024

Performance Highlights

- Large-cap stocks soared in the quarter, with growth stocks handily outpacing value. In this environment, the Westwood Quality Value Fund returned 7.56% but trailed the Russell 1000 Value benchmark, which gained 8.99%.
- Similar to the fourth quarter, large-cap stocks, especially those involved with artificial intelligence (AI), led performance across the broad equity market. However, the rising tide continued to be concentrated and did not lift all stocks evenly. Earnings growth was relatively strong overall, but investors are getting pickier when it comes to results and forward guidance as growth expectations are rising alongside topline economic conditions. This led to wider disparities in individual equity performance, and a bit of a trickier environment at times. And despite what seems to be an increasingly challenged, yet resilient consumer, headline economic data suggests a relatively strong economy. Investors again favored growth over value across the market cap spectrum.
- Stock selection was the primary reason for underperformance on a relative basis; however, asset allocation was also a negative factor.
- On the positive side, the best-performing sectors on a relative basis were **Consumer Discretionary** and **Consumer Staples**, in both cases due to positive stock selection. Results were supported by double-digit returns from a holdings in discount retailers and a national pizza chain, businesses that do well as consumers retrench and focus on the basics.
- Impacting performance negatively were the **Health Care, Information Technology** and **Real Estate** sectors, again largely due to security selection. Returns in both Health Care and Technology were positive but trailed the benchmark's performance.

Performance Drivers

- Only one sector delivered negative performance in the quarter: Real Estate, where investors remain concerned about higher interest rates impacting valuations and lease renewals. The best-performing sector was Financials, followed by Consumer Discretionary.
- Two national banks were among the top five contributors to performance. **JP Morgan Chase (JPM)** added nearly 20% in the quarter, supported by higher net interest income and good discipline on expenses. **Bank of America Corp. (BAC)** also gained in the quarter amid strong earnings despite revenue results that were slightly below expectations.
- Software giant **Microsoft Corp. (MSFT)** posted strong gains amid ongoing excitement around AI and the company's rollout of their CoPilot AI tool. Pizza retailer **Domino's Pizza (DPZ)** added over 20% after reporting strong earnings driven by increased same-store sales. Last, **Hubbell Incorporated (HUBB)** continued its steady march upward; the company posted strong earnings supported by robust demand for its electrical equipment and other positive signals for the business.
- The top detractor in the quarter was **Apple Inc. (APPL)**, one of the top performers in 2023, which declined after announcing that the company will abandon efforts to build a self-driving vehicle and would instead focus on AI applications. **Ventas Inc. (VTR)**, a REIT focused on senior living communities, declined after issuing weaker guidance for 2024. **VICI Properties (VICI)** fell slightly in the quarter despite reasonable results; the stock fell amid negative sentiment driven by interest rate volatility and an uncertain transaction market.
- **Public Storage Inc. (PSA)** declined amid concerns that the self-storage company would not be able to increase rents through the year. Last, health insurer **UnitedHealth Group Inc. (UNH)** suffered as news of a cyberattack took its toll on both earnings and investor sentiment.

Performance Update

As of March 31, 2024

Trailing Years Performance

	1Q24	YTD	1 Year	3 Year*	5 Year*	10 Year*	Since Inception*
Westwood Quality Value Fund	7.56%	7.56%	18.18%	8.42%	10.16%	9.40%	8.23%
Russell 1000 Value Index	8.99%	8.99%	20.27%	8.11%	10.32%	9.01%	7.95%

*Annualized

Calendar Year Returns

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Westwood Quality Value Fund	31.81%	13.84%	12.11%	-0.91%	16.10%	30.03%	11.85%	-0.36%	10.93%	20.85%	-6.04%	27.36%	2.73%	23.79%	-5.66%	8.91%
Russell 1000 Value Index	36.85%	19.69%	15.51%	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%

Inception date is 6/28/06. **The performance data quoted represents past performance. Past performance is not indicative of future results. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. For performance data current to the most recent month end, please call 877.FUND.WHG.** Expense ratio for the fund is 0.69% (gross) and 0.65% (net). The Advisor has contractually agreed to waive fees and reimburse expenses until March 1, 2024. In the absence of current fee waivers, total return would be reduced.

Potential Risks

Mutual fund investing involves risk, including possible loss of principal. There can be no assurance that the Fund will achieve its stated objectives. Portfolio holdings are subject to change and should not be considered a recommendation to buy individual securities. The Fund pursues a “value style” of investing. If the Adviser’s assessment of market conditions, or a company’s value or prospects for meeting or exceeding earnings expectations is inaccurate, the Fund could suffer losses or produce poor performance relative to other funds or market benchmarks. In addition, “value stocks” can continue to be undervalued by the market for long periods of time, and may never achieve the Adviser’s expected valuation.

Top 10 Holdings as of 3/31/2024

Microsoft Corp.	Goldman Sachs Group Inc.
Bank of America Corp.	American International Group Inc.
Johnson & Johnson	UnitedHealth Group Inc.
JPMorgan Chase & Co.	Honeywell International Inc.
Abbott Laboratories	Becton Dickinson and Co.

Top 10 Holdings represents 27.96% of the total portfolio and represents the ten largest portfolio positions by market value in the Fund as of the period end date. Each quarter, the Westwood Funds use this same objective, non-performance based criteria to select the ten largest holdings. Holdings are subject to change. Current and future portfolio holdings are subject to risk.

Fund Positioning and Trade Rationale

Positions were initiated in the following companies:

- **Charles Schwab Corporation (SCHW):** We believe the company has a long runway of asset growth ahead as they gain share with their dual-channel approach and low-cost positioning. We also appreciate the low capital intensity of their business model and ability to reduce expenses following the TD Ameritrade merger. As the Federal Reserve appears to no longer be tightening, we believe deposit costs and flows should stabilize. If interest rates decline, the company should be less sensitive to credit deterioration than other banks.
- **Darden Restaurants (DRI):** The company is one of the leading full-service restaurant chains with brands such as Olive Garden, Longhorn Steakhouse, Yard House and The Capital Grille. We believe Darden's restaurants have pricing power that will allow them to drive a value gap versus peers and maintain steady market share gains. They show visible high single-digit after-tax growth and a 3% dividend, providing the potential for double-digit shareholder returns, an attractive reward to risk profile compared to their industry.
- **Littelfuse, Inc. (LFUS):** Littelfuse is a specialty maker of fuses, relays, temperature monitors and other circuit protection devices for auto, electronic and industrial end markets. Shares are down roughly 25%, providing an attractive reward-to-risk entry point. We believe concerns about customer destocking are overwrought, and we expect to see a return to growth aided by design wins across all three segments. The long-term secular growth driver of electrification remains intact, and the company maintains an attractive profile of low leverage and strong free cash flow generation.
- **Valero (VLO):** One of the top operators of refineries in the country. The company has a strong financial proile with minimal debt, strong cash generation and a commitment to return cash to shareholders. The company's position in renewable diesel is a competitive advantage, and the reward-to-risk profile is attractive given the double-digit free cash flow yield.

The following positions were sold from the portfolio:

- We sold our position in **Public Storage (PSA)**. With occupancy rates moving down and our growing belief that storage demand may continue to decline, we are reallocating proceeds to higher-conviction opportunities.
- We eliminated our position in **Gilead Sciences, Inc. (GILD)** to rotate proceeds into higher-conviction ideas with greater upside potential.
- We sold our position in **Ventas (VTR)**, the senior housing REIT. While we are still optimistic on supply/demand trends in senior housing, we are concerned that the firm's higher cost of capital will create hurdles to their long-term growth potential.

Market Review

Equity markets experienced overall growth in the first quarter of 2024, with both the Dow Jones Industrial Average and the S&P 500 setting record highs in the quarter. The closely watched S&P 500 returned 10.6%, marking the second quarter in a row of double-digit gains and reaching a new high of 5,245 in March. Broad-based market optimism, confidence in corporate earnings and any "landing" still to come in the economy fueled those markets. Large-cap stocks continued to outpace small-cap issues, though small- and mid-cap stocks enjoyed a strong March. From a style perspective, growth outperformed value over the entire market cap spectrum.

Bond markets trended sideways to lower as resilient economic data and sticky inflation prompted a revival in the “higher for longer” interest rate case that was confirmed by the Federal Reserve in their March meeting. Despite the shift in the Fed’s sentiment, investors continued to believe in a benign risk environment.

Technology stocks performed well, driven by increased demand for digital services and the positive outlook on innovation, technology adoption and AI. Energy was the second-best performing equity sector in the quarter, as concerns over the Middle East conflict kept oil and natural gas prices high. The Financials and Industrials sectors also saw significant gains, buoyed by the broader economic recovery and increased infrastructure spending.

The Magnificent 7 led the way for all stocks as AI remained a tremendous catalyst for earnings growth across a myriad of stocks and sectors. The Magnificent 7 were responsible for 40% of the S&P 500's year-to-date gain, compared to more than 60% last year.

The bond market was not as bullish as we saw late last year, but showed signs of stabilization, with yields on government bonds remaining relatively steady. The 10-year Treasury yield, a key indicator for borrowing costs, closed the quarter at 4.20%, up from its final read in 2023 of 3.88%. The decline in the Treasury bond market reflects the Federal Reserve’s cautious approach to interest rate cuts, now expected to total just three for the rest of the year, less than half of what was expected in early January. Corporate bond yields, on the other hand, experienced a slight increase, reflecting the improved credit outlook for many companies and the overall optimism in the market.

In the U.S. economy, the first quarter saw a significant uptick in job creation, as over 1.5 million jobs were added across various sectors, most notably in technology, health care and manufacturing. This level of job creation points to a resilient and adaptable economy. On the other hand, there were an increasing number of layoffs and cost-cutting actions by companies large and small. Nearly 40% of business leaders surveyed by ResumeBuilder believe layoffs are likely at their companies this year, and about half say their companies will implement a hiring freeze.

Consumer spending remained strong in January and February, indicating relative confidence among the American public, with a notable increase in spending on durable goods. The housing market experienced a slowdown in price appreciation, suggesting a shift toward a more balanced market, though demand for housing remained healthy. Low-rate mortgage owners are staying put, restricting supply for now.

Global economic recovery efforts, particularly in major trading partners like the EU and China, have positively influenced American exports, contributing to the growth in manufacturing jobs and sectors reliant on international trade, but the relative economic health of many of our trading partners remains delicate. Recessions are occurring in the U.K., Finland and Ireland, and negative GDP rates for Q4 2023 were also reported in Germany and Canada.

International stocks are positive on the year but are also showing divergence across regions and countries. The MSCI ACWI ex-U.S. Index was up 4.3% in the quarter, while the MSCI Emerging Markets Index gained 2.2%. Within developed international markets, Japan was certainly a standout, despite economic fragility and rising interest rates. Japan’s Nikkei 225 recaptured a high last made 35 years ago as the Bank of Japan increased its short-term borrowing rate for the first time in 17 years. Japanese companies continue to benefit from corporate reforms and a very weak yen, weighed by years of easing monetary policy.

Outlook

We maintain a cautiously optimistic outlook for both stocks and bonds for the coming year. While not as dovish as many might have hoped, it appears the Fed will begin lowering rates at a slow pace around mid- to late-2024 as long as inflationary pressures remain in check. The jury is still out on two or three cuts this year, and we are leaning more toward the former.

Headline consumer data suggests optimism, but we remain concerned about housing costs, depleted savings and record high-rate credit card debt. And while easing inflation is good for consumers, it reduces pricing power and margin growth for companies. Earnings growth should continue to accelerate into 2024, assuming lower rates into the back half of the year.

With equity valuations elevated, multiple expansion from here forward is less likely and could limit the appeal of pure “beta” exposure. Earnings growth would become the main driver of stock returns as we look ahead. Specifically, we seek to identify businesses with underappreciated earnings potential, as we believe those companies will be rewarded as their stock is trading cheaper than printed estimates imply.

Important Information