

Small Cap Quality Growth Portfolio | Fourth Quarter 2023

Strategy Objectives

1. Price appreciation: Compelling alpha and Sharpe ratio since inception
2. Downside protection: Competitive daily downside capture¹
3. Income: 1.5% yield²

4Q2023 Results Relative to Strategy Objectives:

Price Appreciation

- During 4Q2023 the strategy's small cap, dividend growth-focused mandate performed in line with the Russell 2000 Growth benchmark.
- Year-over-year inflation rates continued to fall in support of the Fed's five-month, and counting, pause in interest rate hikes. In December, the Fed embraced a dovish tone, suggesting a cut may be the next move in rates, which propelled interest rate sensitive equities in the final days of the quarter.
- As the market embraced a more risk-on stance during the quarter and discounted the probability of recession, traditionally cyclical corners of the Russell 2000 Growth, including the Communication Services sector and the biotechnology industry, outperformed.
- We remain convicted in the outlook for risk-aware, active small capitalization strategies with a focus on sustainable dividends and stable fundamentals as we enter 2024. While there is optimism surrounding the Fed's 4Q2023 pivot language, the current environment is still defined by the tightest monetary conditions in the last decade which we believe presents an opportunity for quality companies with strong balance sheets to outperform.

Downside Protection

- Daily downside capture of 66.4% and 70.4% across all negative Russell 2000 Growth and Russell 2000 days, respectively, in the quarter-to-date period ended 12/31/2023. During the quarter, the strategy also delivered daily upside capture of 73.9% and 74.7% across all positive Russell 2000 Growth and Russell 2000 days, respectively.¹

Income

- 7 strategy holdings announced dividend hikes with an average TTM increase of +7.2%, signaling continued business stability and financial health of the portfolio. The strategy remains positioned for broad-based dividend growth going into 2024.

4Q2023 Dividend Increases		
Company	TTM % Increase	Current Yield
Avient (AVNT)	4.0%	2.5%
Balchem (BCPC)	11.3%	0.5%
Ensign Group (ENSG)	4.3%	0.2%
Innospec (IOSP)	10.8%	1.2%
Lancaster Colony (LANC)	5.9%	2.2%
Power Integrations (POWI)	11.1%	1.0%
Stepan (SCL)	2.7%	1.6%

Source: Bahl & Gaynor and FactSet, 2024.

4Q2023 Trades Executed	
Initiations	Eliminations
Avnet (AVT)	TTEC Holdings (TTEC)
Increases	Reductions
BWX Technologies (BWXT)	Avient (AVNT)
CSG Systems (CSGS)	Evercore (EVR)
Lancaster Colony (LANC)	Exponent (EXPO)
MSA Safety (MSA)	Inter Parfums (IPAR)
U.S. Physical Therapy (USPH)	Stepan (SCL)

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Portfolio Review

The Small Cap Quality Growth portfolio performed in line with the Russell 2000 Growth Index in 4Q2023. Stock selection within Industrials and Materials and an underweight in Energy contributed positively to performance. Stock selection within Health Care and Financials, and an underweight in Information Technology detracted from performance.

The largest positive drivers of current quarter performance included:

- Strong stock selection in Industrials through the ownership of high-quality, dividend paying companies in the industrial machinery & supplies, building products, and construction machinery industries contributed positively to strategy performance.
- No ownership of integrated oil & gas companies within Energy and selective ownership of midstream companies contributed positively to strategy performance as oil prices continued to fall from September highs. Energy companies further removed from exploration & production and direct refining performed better during the period which was a benefit to strategy holding World Kinect (WKC).
- Ownership of select specialty chemicals companies within Materials contributed positively to performance. While destocking headwinds continued to pressure volumes throughout the industry, the strategy holdings were able to post better-than-expected margin profiles with upside going into next year.

The largest negative drivers of current performance included:

- Ownership of over-the-counter pharmaceutical manufacturer Perrigo (PRGO) and no ownership of the largely unprofitable biotechnology industry within Health Care detracted from strategy performance. This was partially offset by an above average weight in healthcare services company Chemed (CHE) and healthcare facilities company Ensign (ENSG), both of which exhibited robust fundamentals.
- Within Financials, ownership of property and casualty company Kinsale (KNSL) and asset manager Victory Capital (VCTR) contributed negatively to performance. This was partially offset by ownership in regional banks which rebounded from October lows following a shift in the interest rate narrative.
- No ownership of application and internet software within Information Technology detracted from performance; this was partially offset by ownership of Universal Display Corp (OLED) which continued to see enthusiasm for its display panel technology.

Largest Portfolio Contributors

1. **Federal Signal (FSS):** In addition to robust continued demand across its unique product portfolio, the company is benefiting from previous capacity expansion investments and supply chain initiatives. Strong order trends combined with elevated backlog and improving production rates have supported accelerated growth and attractive incremental margins.
2. **EnPro (NPO):** Through strong margin performance and solid results to other end-markets, NPO has been able to mitigate headwinds related to lower aggregate CAPEX across the semiconductor industry. This, in addition to optimism for an accelerated recovery in semiconductor spending, has contributed to recent outperformance.
3. **MDC Holdings (MDC):** Amid mortgage rate volatility, MDC applied incentives and utilized rate buy-downs to drive robust sales growth during 2023. The company's long-term outlook remains bright given a favorable macro environment with limited housing supply, its strong balance sheet, and a demonstrated commitment to dividend growth.

Largest Portfolio Detractors

1. **Kinsale (KNSL):** KNSL posted below consensus gross written premium growth in 3Q2023, pressuring shares following strong performance in 2023. The company's technology advantage allows for through-cycle profitability, regardless of market demand or pricing dynamics.
2. **U.S. Physical Therapy (USPH):** Profit margins were pressured during USPH's most recent quarter driven by lower net reimbursement rates from Medicare, weakness in the company's industrial prevention business, and many recently acquired and de novo clinics that are yet to mature into USPH-like profitability. Despite these headwinds, USPH is well positioned for continued organic and inorganic market share growth given its pristine balance sheet versus peers.
3. **Perrigo (PRGO):** As a generics and over-the-counter manufacturer, the sustainability of PRGO's margin profile remained in question due to its private label brands and input cost inflation. However, PRGO's portfolio is compelling through-cycle if consumers trade down in a slowing economy; it is further supported by high-growth and high-margin segments like women's health and skin care.

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Strategy Style Categorization

Asset Class	Benchmarks	Mandate
Domestic Equity	Russell 2000 Growth & Russell 2000	Small Cap Growth

Investment Philosophy

Bahl & Gaynor employs a 'Growth at a Reasonable Price' discipline to purchase high-quality companies at sensible valuations. It is our goal to seek competitive performance while preserving capital in declining markets. In addition, our focus on companies that pay a growing dividend has benefited our clients in the form of a reliable income stream.

We are long-term investors and seek to identify companies that are managed conservatively and for growth, have stable and sustainable business models, and reward shareholders with a growing dividend. It is our intention to identify the best companies that meet these criteria and hold them for long periods of time.

Bahl & Gaynor's investment philosophy exemplifies our firm belief in the power of long-term investing and compounding dividend income.

Small Cap Quality Growth Positioning

Our Small Cap Quality Growth strategy focuses on owning small-size companies having market capitalizations, at the time of investment, within the range of the market capitalizations of the Russell 2000 Index. Protection of capital in falling markets, providing an above-average income stream, and strong performance relative to the index and other small-cap managers, embody the strategy's goals.

Bahl & Gaynor's equity selection process yields an investable universe of companies that are managed conservatively and for long-term growth, have stable and sustainable business models, and currently reward shareholders of the company with a dividend.

Over a full market cycle, Bahl & Gaynor's Small Cap Quality Growth strategy seeks to outperform its benchmark and small-capitalization growth peers all in the context of a lower-than-average portfolio risk profile.

Client portfolios will generally be diversified among small capitalization common stock with each security typically held for three to five years. Low portfolio turnover combined with the favorable tax treatment of dividend income results in a cost and tax-efficient portfolio.

Portfolio Management Parameters

1

Companies initiated in the portfolio pay a cash dividend at the time of purchase

2

Portfolio typically managed to maximum 5% capital contribution per stock

3

Cash is non-tactical and typically represents 0% to 3% of portfolio value

4

Under normal circumstances, at least 80% of the strategy's net assets are invested in stocks of small capitalization companies with market capitalizations within the range of the market capitalizations of the Russell 2000® Index

5

Annual portfolio turnover is low to moderate

6

Sell or trim decisions are based upon fundamentals, dividend policy, and better opportunities

7

The strategy employs no derivatives, exchange-traded funds or mutual funds

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Portfolio Details

Sector	Small Cap Quality Growth Weight	Russell 2000 Growth Weight	Russell 2000 Weight	Top 10 Holdings	Small Cap Quality Growth Weight
Industrials	34.0%	19.4%	17.0%	Ensign Group (ENSG)	5.54%
Health Care	19.8%	21.8%	15.0%	Chemed (CHE)	5.34%
Financials	13.3%	7.1%	18.5%	Federal Signal (FSS)	4.26%
Consumer Staples	7.7%	4.4%	3.4%	Curtiss-Wright (CW)	4.01%
Information Technology	7.4%	24.7%	15.6%	UFP Industries (UFPI)	3.96%
Materials	7.3%	4.5%	4.7%	Tetra Tech (TTEK)	3.94%
Real Estate	2.8%	0.8%	4.4%	Inter Parfums (IPAR)	3.46%
Utilities	2.1%	1.5%	2.8%	Evercore (EVR)	3.45%
Consumer Discretionary	2.1%	10.4%	11.2%	Enpro (NPO)	3.32%
Communication Services	1.3%	1.4%	1.5%	U.S. Physical Therapy (USPH)	3.28%
Energy	0.9%	3.9%	5.9%		
Money Market	1.3%	-	-		

Portfolio Statistics	Small Cap Quality Growth WRAP (Pure Gross)	Russell 2000 Growth	Russell 2000
P/E Ratio (trailing 12 months)	24.5x	21.5x	14.5x
P/B Ratio	3.0x	4.0x	2.0x
Weighted Average Market Cap	\$5.1 B	\$3.8 B	\$3.2B
Dividend Yield – Gross of Fees ²	1.5%	0.6%	1.4%
B+ or better S&P Quality Ranking	51.4%	15.9%	19.5%
Beta since inception (Gross / Net)	0.78/0.78	1.00	0.96
Sharpe ratio (Gross / Net)	0.50/0.32	0.33	0.31

Source: FactSet, 2024. Inception date 12/31/2005. Beta figures are relative to Russell 2000 Growth Index.

4Q2023 Performance (Annualized)	Small Cap Quality Growth WRAP (Pure Gross)	Small Cap Quality Growth WRAP (Net)	Russell 2000 Growth	Russell 2000
1 Year	19.45%	15.93%	18.66%	16.93%
3 Years	6.56%	3.42%	-3.50%	2.22%
5 Years	11.59%	8.30%	9.22%	9.97%
10 Years	9.04%	5.83%	7.16%	7.15%
15 Years	13.46%	10.12%	12.07%	11.30%
Since Inception	10.15%	6.91%	8.18%	7.77%

Source: Bahl & Gaynor, Informa – PSN, 2024. Inception date 12/31/2005.

4Q2023 Risk (Annualized)	Small Cap Quality Growth WRAP (Pure Gross)	Small Cap Quality Growth WRAP (Net)	Russell 2000 Growth	Russell 2000
1 Year	19.09%	18.78%	22.85%	23.19%
3 Years	19.12%	19.24%	21.79%	21.11%
5 Years	20.12%	20.29%	24.20%	24.02%
10 Years	17.37%	17.50%	20.59%	20.16%
15 Years	17.45%	17.46%	20.63%	20.42%
Since Inception	17.46%	17.46%	20.85%	20.43%

¹Source: Bahl & Gaynor; historical downside (upside) capture is the sum of strategy returns on all Russell 2000G and Russell 2000 down (up) days divided by the sum of index returns on all respective down (up) days. Down (Up) days are defined as any trading day the index posts a negative (positive) total return. Strategy performance is derived from the internal rate of return (IRR) of a single non-fee paying representative/model account.

²Dividend yield includes cash holdings.

Source: FactSet, 2024, Bahl & Gaynor. Statistics and weight data is drawn from the Small Cap Quality Growth model portfolio that is fully discretionary, unconstrained and subject to change. Individual Bahl & Gaynor clients may or may not hold these positions or have similar characteristics. Risk and return data are representative of the Small Cap Quality Growth WRAP composite. **Past performance does not guarantee future results.** Other methods may produce different results and the results for individual accounts and for different periods may vary depending on market conditions and the composition of the account. Care should be used when comparing these results to those published by other investment advisers, other investment vehicles and unmanaged indices due to possible differences in calculation methods. No alteration of the composite as presented here has occurred because of changes in personnel or other reasons at any time.

Standard & Poor's (S&P) Quality Ranking: S&P determines "quality" via a company's 10-year history of earnings growth and dividend growth. Those with a quality rating of B+ (or better) are considered "average" (or better).

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Thanks

Your continued support and interest are much appreciated.

Everyone at Bahl & Gaynor would like to thank you for the opportunity to serve your investment needs.

If you would like to speak in greater detail with a member of the B&G Team, please reach out to us through our Institutional Consulting Group.

Contact Us

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