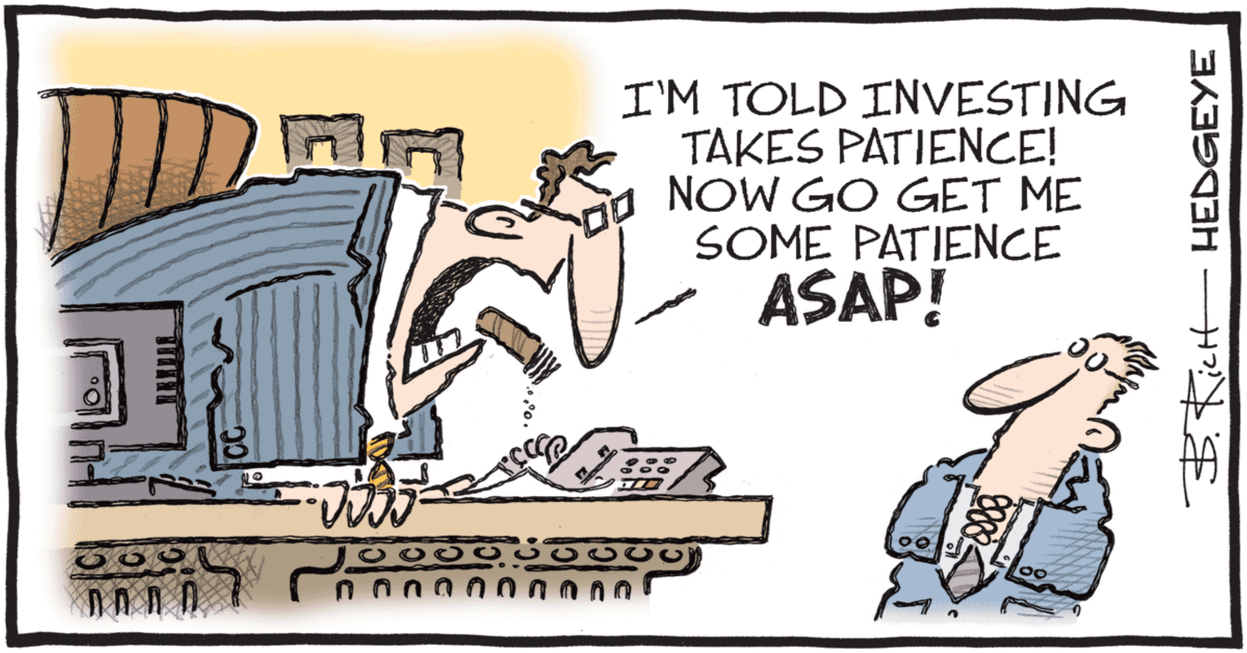
HAHN CAPITAL MANAGEMENT, LLC
REGISTERED INVESTMENT ADVISORS

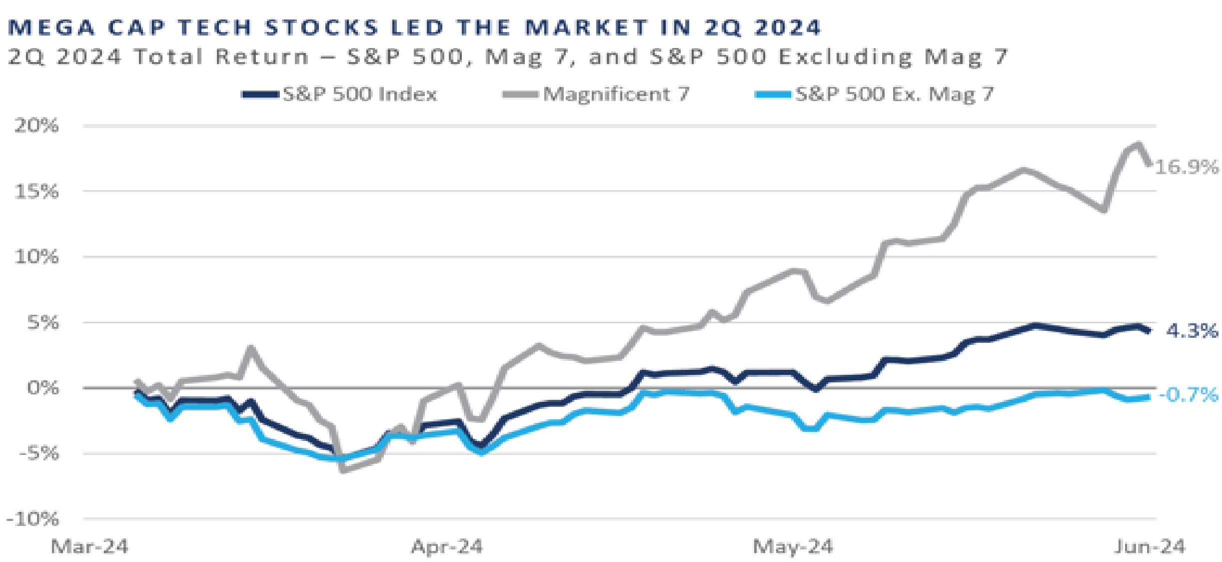
Mid Cap Equity Strategy **2nd Quarter 2024 Commentary**



Source: Hedgeye

It's a Big World

Despite stumbling out of the gates early in the quarter, the S&P 500 Index quickly regained its footing to post a 4.3% total return, adding to an impressive year-to-date gain of 15.3% and setting fresh record high levels along the way. Indeed, the Bloomberg Magnificent 7 Index posted a 16.9% total return for the quarter and a staggering 37.0% for the first half of the year, versus mediocre performance by the remaining 493 constituents of the S&P 500, which saw a decline of 0.7% in the second quarter and a relatively more modest return of 8.6% for the first half of 2024.

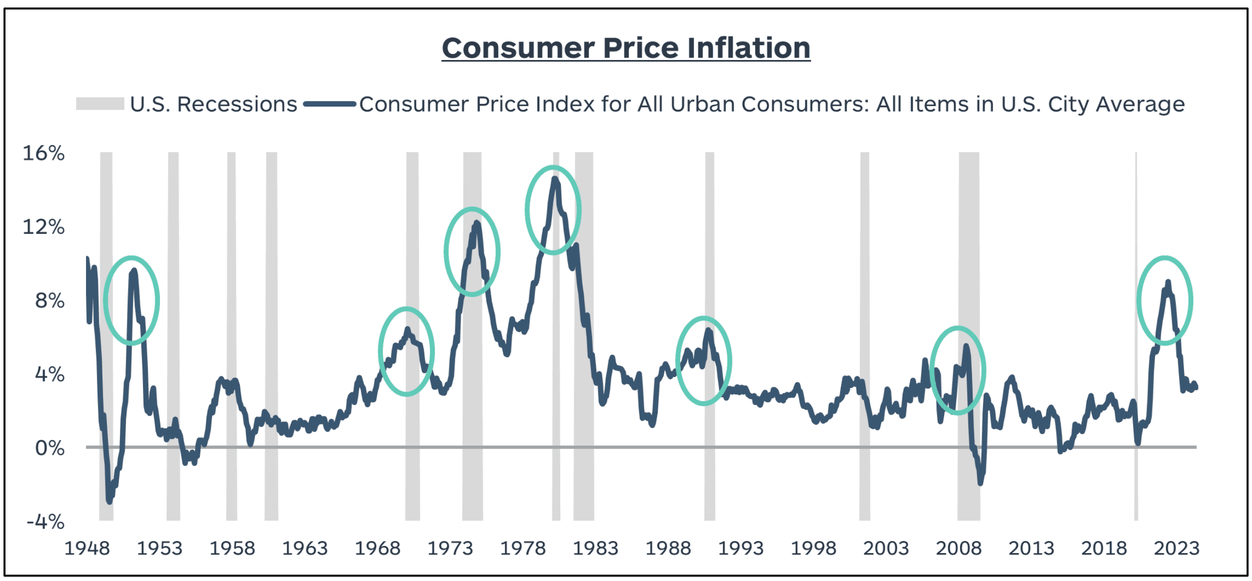


Data source: Bloomberg, L.P.; Data as of June 30, 2024

Putting the "Soft" in "Soft Landing"

After sticky inflation captured most of the focus in the first quarter, the second quarter brought some relatively weaker economic data that called into question key areas of economic resilience. While not quite enough to convince the Federal Reserve (Fed), markets seemed to take moderating labor markets and consumer spending as a sign that inflation will remain suppressed enough for rate cuts to begin later this year. In the meantime, while certain interest-rate sensitive pockets of the economy struggle, and others move from "very strong" to "strong," overall economic activity continues to chug along. As of late June, the Atlanta Fed's GDPNow model is tracking 1.7% growth in the second quarter (Q2), which would be a modest acceleration from the first quarter (Q1), when weak inventories and net exports limited growth to 1.4%.

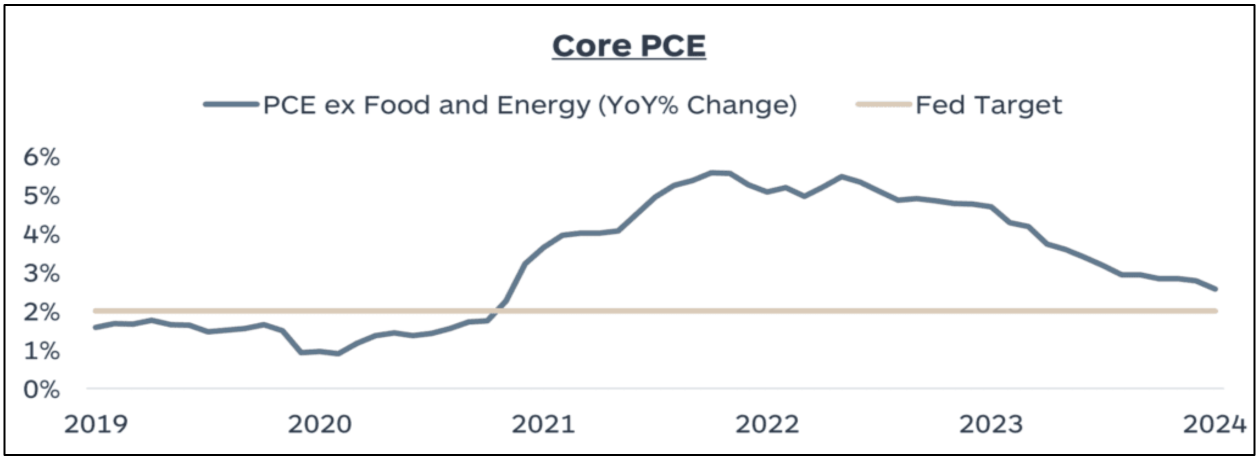
Reflecting on how far we've come, we must take a moment to acknowledge the relatively painless nature of the disinflation we have seen so far. After all, the U.S. economy saw the year-over-year Consumer Price Index (CPI) go from its peak of +9% in June 2022 back down to +3%, all while adding over $1 trillion (inflation-adjusted) to annual economic output, as well as over 100,000 new jobs each month along the way. This is not typical. Usually, when inflation spikes meaningfully, a recession is required to put a lid on price increases and ultimately push inflation back down. The last exception to occur was in 1951. Back then, supply disruptions from the Korean War and a rush of demand from consumers with fresh memories of WWII rations sent year-over-year CPI to near 10%. After solidifying its independence with the Treasury-Fed Accord in 1951, the Fed was able to regain control of interest rates that had been pegged artificially low to protect the value of war bonds. After rates were allowed to rise, inflation was back down to 2% by March 1952 and no recession was required.



Source: FRED

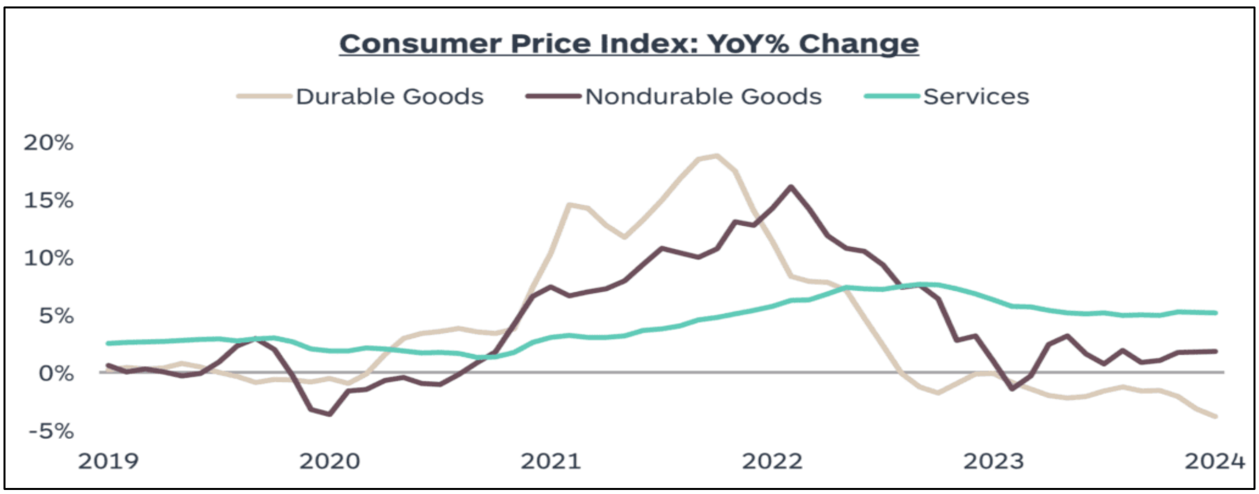
Since then, we've seen six cases of year-over-year CPI breaching 5% (including in 2021). In the first five instances, inflation didn't peak until a recession had already begun. So, at least within this context, "this time" has *already* been "different."

Of course, none of this says much about what to expect as we navigate the "last mile." Q2's three CPI releases all began with a "3," while the Fed has been clear that its goal for inflation is 2.0% (although Fed Chair Jerome Powell seems to be communicating that confidence in "a sustainable path to 2.0%" may be enough to begin easing policy). Fortunately, the core Personal Consumption Expenditures (PCE) price index (the Fed's preferred inflation metric) is closer to the target at 2.6% as of the end of May.



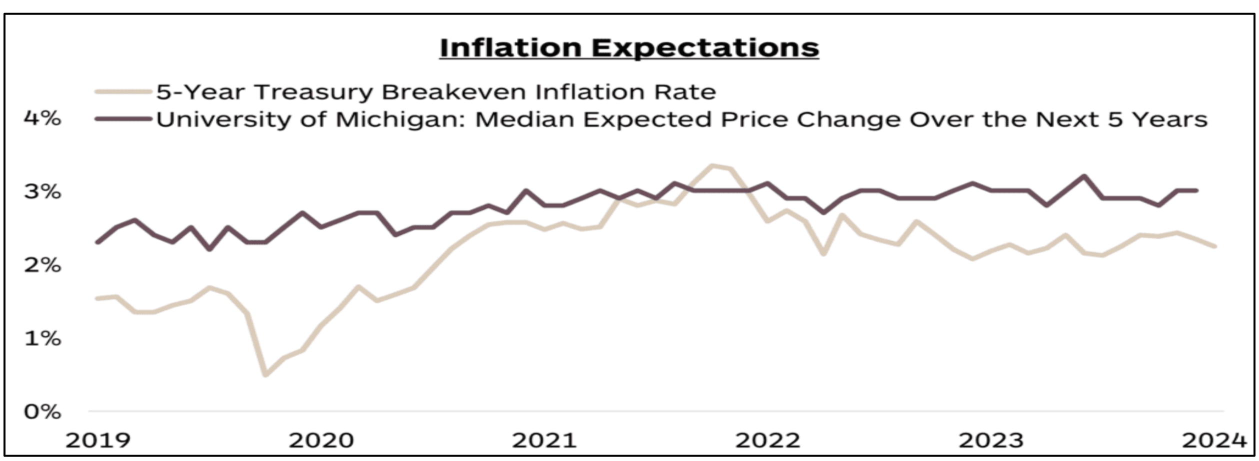
Source: FRED

With durable goods prices back to their longer-term deflationary trend, what is left behind are stickier components like shelter and services. Shelter inflation is currently being supported by housing shortages and measurement quirks, while services inflation is reacting to resilient consumer demand and solid wage growth (a major cost for service-related industries).



Source: FRED

Despite the recent bump along the road to 2%, longer-term inflation expectations remain anchored near recent historical averages.

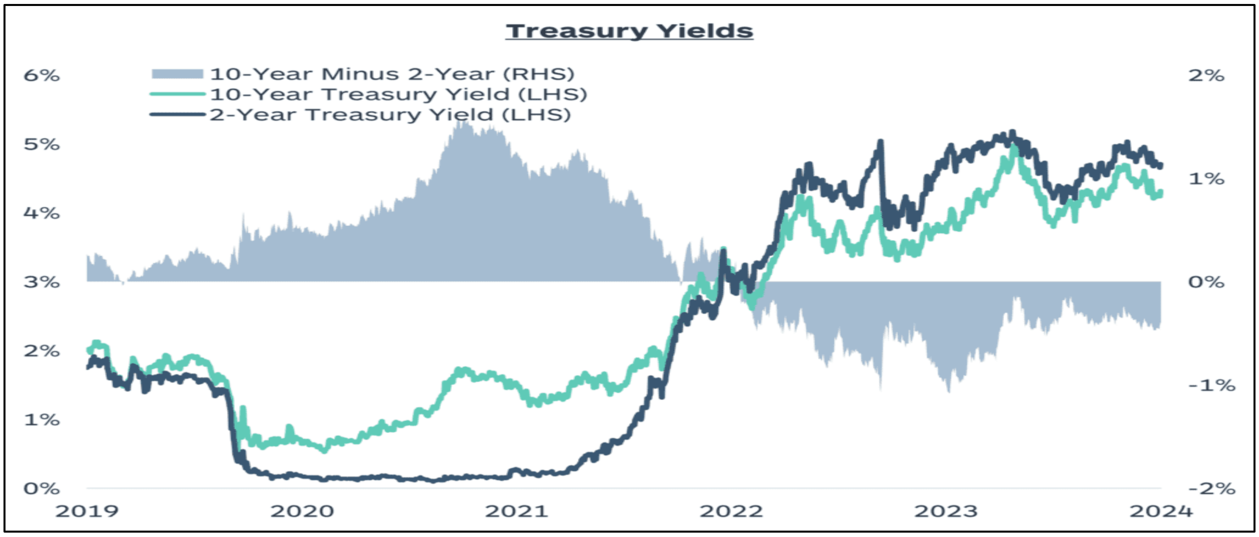


Source: FRED, University of Michigan

Awaiting the Cutting Cycle

While policy rates were held in place during the quarter, the June Federal Open Market Committee (FOMC) meeting brought with it a new Summary of Economic Projections (aka "dot plot"). The latest release revised the FOMC's median expectations for rate cuts in 2024 from three down to one (with a range of zero to two). The committee's latest communication largely confirms the progression of market pricing in federal funds futures, which had gone from expecting six 2024 rate cuts in the beginning of the year all the way down to one or two.

Despite delayed rate-cutting plans, weakening economic data helped put a stop to the rise in longer-term interest rates. In April 10-year U.S. Treasury yields peaked at 4.70% and moved lower throughout the rest of the quarter. By June 30, yields had settled at 4.37%.

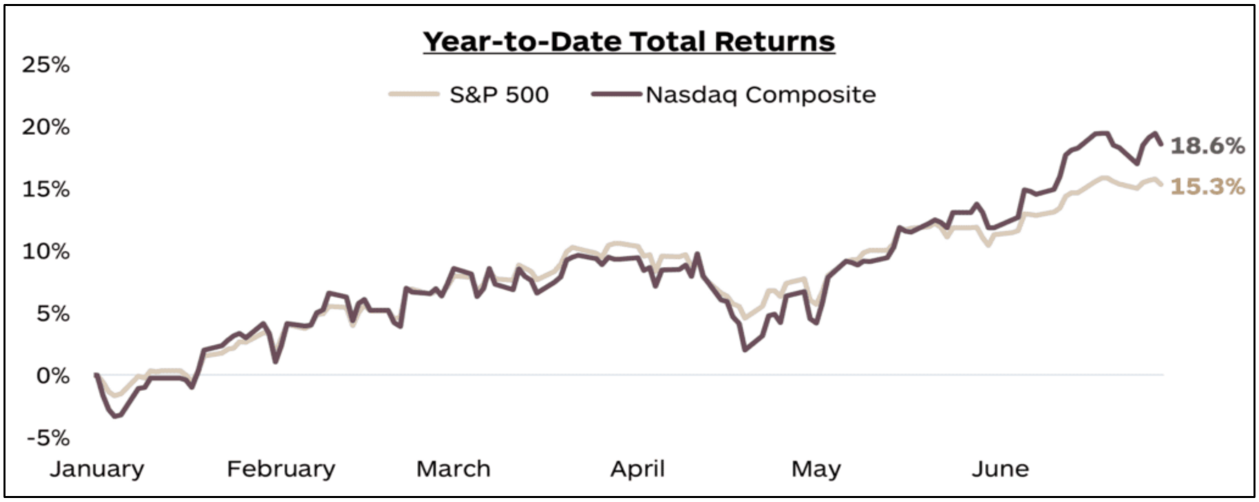


Source: FRED

With the 2-year U.S. Treasury yield at 4.72%, yield curves remain stuck in inversion. Often, inverted yield curves are resolved by way of rapidly falling short-term rates as some type of economic shock requires swift policy easing. As we pass the two-year inversion anniversary without such a crisis, short rates continue to reflect plans for a slow and steady easing cycle. Longer-term rates are attempting to balance the concepts of eventually lower short rates with sticky inflation and increasing future Treasury bond supply to finance large fiscal deficits.

"Haves" and "Have Nots" in the Equity Markets

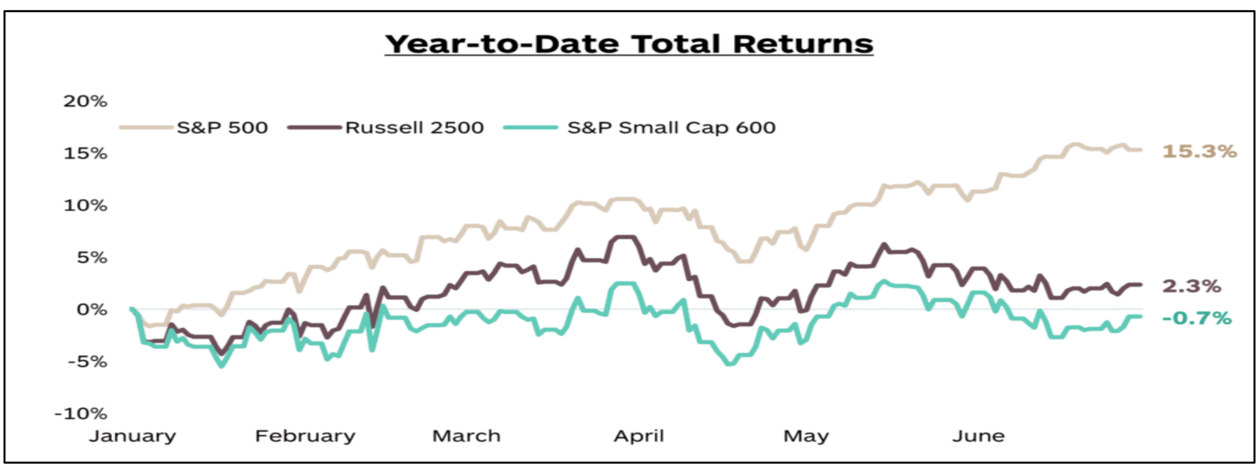
Equity markets posted a solid quarter at the headline level, but the story of limited breadth continues under the surface. Large cap technology stocks continue to forge along, emboldened by the game-changing promise of artificial intelligence (AI).



Source: Bloomberg

The proliferation and mind-boggling pace of progress for large language models like OpenAI's ChatGPT have started an arms race amongst "hyper-scalers" who rush to build data centers and fill them with the graphics processing units needed to process large amounts of data. The main beneficiary? Nvidia, of course. The company's stock gained another 37% during the second quarter, driving its market cap past $3 trillion, which was briefly enough to dethrone Microsoft as the world's most valuable company. Though its valuation is by no means cheap, the company has again been able to back up its eye-popping stock performance with earnings growth of almost 600% year-over-year.

While the "AI trade" pulled the tech-heavy Nasdaq composite to an 8% quarterly total return, the average large cap stock (as defined by the S&P 500 Equally Weighted Index) was down 3% for the quarter. Meanwhile, smaller stocks continue to struggle, with the "smid cap" Russell 2500 Index down 4% and the "small cap" S&P 600 Index down 3% in the quarter.



Source: Bloomberg

Quarterly Performance

The return for the Hahn Capital Management Mid-Cap Value Composite was ***-3.95% gross of fees and -4.20% net of fees in the second quarter of 2024***. For the quarter, we underperformed our primary benchmark, the Russell Mid-Cap Value Index, by 0.55 percentage points gross of fees and underperformed by 0.80 percentage points net of fees.

For the quarter, in the representative account, sector allocations to Industrials, Financials, Consumer Staples, and cash contributed, while those to Real Estate, Information Technology, and Health Care detracted.

In the representative account, the most significant relative performers during the quarter were WabTech(WAB), EMCOR Group (EME),Virtu Financial (VIRT), and Ross Stores)ROST), while the most significant underperformers were Keysight (KEYS), PVH Corp. (PVH), CBRE Group (CBRE), and Alexandria Real Estate (ARE).

Hahn Capital Quarterly Performance Attribution – 2Q 2024

LINKED PERFORMANCE BY SECTORS

BENCHMARK: Russell Midcap Value Index
PORTFOLIO: Representative Account

GICS Sector	PORT Weight	BENCH Weight	DIFF Weight	PORT Return	BENCH Return	DIFF Return	SECTOR SELECT	STOCK SELECT	ACTIVE CONTR	PASSIVE CONTR	TOTAL CONTR
Financials	19.61%	18.02%	1.60%	-1.10%	-3.25%	2.15%	0.01%	0.40%	0.41%	0.00%	0.41%
Information Technology	6.45%	9.39%	-2.94%	-7.35%	1.45%	-8.80%	-0.14%	-0.57%	-0.71%	0.00%	-0.71%
Real Estate	13.41%	9.82%	3.59%	-4.68%	0.84%	-5.53%	0.15%	-0.72%	-0.57%	0.00%	-0.57%
Industrials	23.02%	20.47%	2.55%	-0.82%	-5.01%	4.20%	-0.05%	0.93%	0.88%	0.01%	0.89%
Health Care	13.03%	6.26%	6.77%	-7.95%	-7.96%	0.01%	-0.32%	0.02%	-0.30%	0.00%	-0.30%
Consumer Discretionary	6.89%	9.03%	-2.14%	-10.00%	-7.04%	-2.96%	0.09%	-0.25%	-0.16%	0.00%	-0.16%
Materials	1.34%	7.48%	-6.14%	-23.32%	-7.90%	-15.42%	0.30%	-0.27%	0.03%	0.00%	0.03%
Communication Services	5.36%	2.83%	2.53%	-1.01%	-2.37%	1.37%	0.04%	0.03%	0.07%	0.00%	0.07%
Energy	3.76%	5.59%	-1.84%	-2.66%	-1.90%	-0.77%	-0.03%	-0.03%	-0.06%	0.01%	-0.05%
Consumer Staples	0.27%	3.60%	-3.33%	-2.26%	-8.57%	6.31%	0.17%	-0.02%	0.15%	0.00%	0.15%
Utilities	0.00%	7.50%	-7.50%	0.00%	3.61%	-3.61%	-0.49%	0.00%	-0.49%	0.00%	-0.49%
Cash	6.85%	0.00%	6.85%	1.37%	0.00%	1.37%	0.30%	0.00%	0.30%	0.00%	0.30%
Total Portfolio - Net of Fees				**-3.83%**	**-3.40%**	**-0.43%**	**0.04%**	**-0.46%**	**-0.42%**	**-0.01%**	**-0.43%**

Relative Performance by Stock – Quarter Ended June 30, 2024

Quarter Ended 06/30/2024 - Representative Account vs Russell Midcap Value Index

Top Four Holdings Total Attribution			Bottom Four Holdings Total Attribution			Top Four Sectors Total Attribution			Bottom Four Sectors Total Attribution		
1	WABTEC CORP	0.66%	1	KEYSIGHT TECHNOLOGIES IN	-0.52%	1	Industrials	0.89%	1	Information Technology	-0.71%
2	EMCOR GROUP INC	0.47%	2	PVH CORP	-0.50%	2	Financials	0.41%	2	Real Estate	-0.57%
3	VIRTU FINANCIAL INC-CLASS A	0.41%	3	CBRE GROUP INC - A	-0.35%	3	Not Classified	0.30%	3	Utilities	-0.49%
4	ROSS STORES INC	0.27%	4	ALEXANDRIA REAL ESTATE EQU	-0.33%	4	Consumer Staples	0.15%	4	Health Care	-0.30%

HCM MID-CAP VALUE COMPOSITE PERFORMANCE HISTORY

% Annualized Returns As of 06/30/2024	2Q 2024	1 Year	3 Years	5 Years	7 Years	10 Years	Since Inception 06-30-88
HCM Gross of Fees	**-3.95%**	**11.29%**	**0.25%**	**6.68%**	**7.97%**	**7.24%**	**12.99%**
HCM Net of Fees	**-4.20%**	**10.21%**	**-0.75%**	**5.63%**	**6.91%**	**6.18%**	**11.89%**
Russell Mid Cap Value Index	**-3.40%**	**11.98%**	**3.65%**	**8.50%**	**7.67%**	**7.60%**	**10.97%**
Russell Mid Cap Index	**-3.35%**	**12.88%**	**2.37%**	**9.46%**	**9.63%**	**9.04%**	**11.16%**

Link to: HCM Performance Disclosures

PORTFOLIO ACTIVITY

New Positions

Brown Forman Corp. (BFB) – We initiated a position in BFB during the quarter. Brown-Forman Corporation, together with its subsidiaries, manufactures, distills, bottles, imports, exports, markets, and sells various alcoholic beverages. It provides wines, whiskey spirits, whiskey-based flavored liqueurs, ready-to-drink cocktails, ready-to-pour products, vodkas, tequilas, gin, brandy, rum, bourbons, and liqueurs. The company offers its products primarily under the Jack Daniel's, Woodford Reserve, Old Forester, Coopers' Craft, Gentleman Jack, Herradura, El Jimador, Korbel, Sonoma-Cutrer, Finlandia, Chambord, Gin Mare, Diplomático, Fords Gin, The Glendronach, Benriach, Glenglassaugh, and Slane brands.

It is also involved in the sale of used barrels, and bulk whiskey and wine; and provision of contract bottling services. The company serves retail customers and consumers through distributors or state governments, and retailers, wholesalers, and provincial governments directly. It has operations in the United States, Germany, Australia, the United Kingdom, Spain, Canada, France, Mexico, Poland, Brazil, Japan, and internationally. The company was founded in 1870 and is headquartered in Louisville, Kentucky.

Key Drivers of Growth

1. **Strong Brand Portfolio:** Jack Daniel's remains a leader in the whiskey category, with continued strong sales growth. Other brands, such as Woodford Reserve and Herradura, also contribute to overall growth.
2. **International Expansion:** Significant growth in international markets, particularly in Asia and Latin America, where rising disposable incomes and premiumization trends are driving demand.
3. **Digital Transformation:** Investments in digital marketing and e-commerce have enhanced customer engagement and sales channels.
4. **Strategic Acquisitions:** Recent acquisitions and partnerships have expanded the company's footprint and product offerings.

Brown-Forman operates a vertically integrated model, encompassing production, marketing, and distribution. The company's strategy focuses on premiumization, innovation, and global expansion. Key elements of their strategy include:

1. **Premium Branding:** Emphasis on high-margin premium products.
2. **Geographic Diversification:** Expansion in emerging markets, particularly Asia-Pacific.
3. **Sustainability Initiatives:** Commitment to environmental and social responsibility.
4. **Innovation:** Continuous product innovation to capture evolving consumer preferences.

Despite outstanding financial returns, including a return on assets of 10%, we were able to purchase our initial stake in Brown Forman at a 7-year low. We believe that the company can grow revenues by 6-7% per year over the long term and to compound earnings at over 10% annually moving forward. Current headwinds include inventory destocking by retailers and wholesalers as well as some changing consumer preferences and inflation.

Positions Increased

Waner Music Group (WMG) – We added to WMG this quarter as we were pleased with results that they posted in the first quarter.

The music industry is experiencing a significant expansion, with streaming revenues boosted by continued international expansion of subscriber bases for companies like Spotify and Apple Music. In addition, Warner appears to be gaining market share, and its margins are expanding at a healthy clip along with its sustained revenue growth. WMG continues to expand its offerings internationally and acquire additional music catalogs at attractive economics.

Positions Reduced

There were no positions reduced during the quarter.

Positions Sold

Albemarle (ALB) – We sold our position in Albemarle in the second quarter. Despite long-term demand trends for the lithium industry, Albemarle and other industry players have been plagued by low prices for the metal as industry inventories remain high and more global production is expected to come online over the next two years. We may yet revisit Albemarle in the future, but we currently expect that earnings growth will remain depressed for the intermediate term as electric vehicle demand is not currently great enough to offset lithium supply growth.

Outlook

Economic & Market Outlook

The U.S. economy appears to be slowing just enough to revive dormant disinflationary forces, but not enough to provoke fears of recession. Jobs and wage growth should continue to be the primary driver of consumer spending though markets will be monitoring the slight weakness beginning to develop in weekly jobless claims and job openings to see if it leads to meaningful employment declines over the coming quarters. While the more cyclical income effect on consumer spending should always be the primary determinant of its magnitude, a developing secular dynamic supporting spending relates to the wealth effect and the increasing willingness to draw down excess savings, particularly among the recently retired members of the baby-boom generation who will likely continue to spend on experiences within the services economy. Another potential support to economic growth will be the greater fiscal spending that usually occurs in presidential election years when an incumbent is running for reelection. Recently announced student debt relief (if courts allow it to stand) and greater defense spending due to heightened geopolitical risk should make its way through the economy over the summer months.

Businesses have been more restrained than consumers in their year-to-date spending patterns. But with no apparent overbuild in inventories and the need to invest in productivity-enhancing technology applications in a somewhat labor-constrained environment, capital spending should be supportive of economic growth through the remainder of the year. The housing sector has been pressured by high mortgage rates and high prices in a still-somewhat supply-constrained existing home sales market. Oversupply in the multifamily sector of the new homes market will likely be a constraining factor in the growth of the overall sector. A decline in mortgage rates appears to be needed for housing to add to gross domestic product (GDP) growth, but that is not likely to occur until sometime in the fourth quarter.

With secular AI themes, the specter of rate cuts, and rising corporate profits, there are plenty of tailwinds for continued market growth in the second half. Most of these tailwinds seemed to be pulled forward into the first half performance (which was then concentrated into the Mag 7 stocks).

Year to date, only 25% of the S&P 500 stocks have outperformed the market. It seems intuitive that broader participation would make future market gains more sustainable. Even if narrow leadership continues into the second half of this year, stubborn inflation, economic weakness, and election angsts could introduce volatility among the mega cap stocks and the long-awaited opportunity for the rest of the market.

You can believe us when we tell you that we are as frustrated by the relative underperformance of Mid-Cap as you are, the unprecedented valuation expansion of large cap stocks relative to small and mid-cap stocks is not sustainable. The catalyst to close the performance gap can't be known but will certainly occur. We are extremely optimistic about the businesses that we own on your behalf; recent purchases such as Bio-Techne, Warner Music Group and Brown Forman are best-in-class businesses that have great long-term opportunities for growth. The quality of the business in our portfolio remains very high. Thank you for your support.

John Schaeffer
President and CIO

Michael Whitfield
Dir. of Research and Co-Portfolio Manager