DISTILLATE CAPITAL

2023 Q3 Letter to Investors: Avoiding Risk

Letter Summary

We continue to see significant opportunity in equities by being selective in order to avoid two major risks in U.S. equities. In the small cap space, very elevated levels of debt are combining with higher interest rates to substantially eat into profits. Among large caps, valuation has become a key risk as a number of large expensive stocks are dragging down the aggregate free cash flow yield of the broader market. Relative to higher bond yields, the low single digit free cash flow yields on a number of stocks are implicitly pricing in significant future growth. Should actual growth fall short of lofty embedded expectations, those stocks or even some portion of them would be at significant risk and given their size, would have a deleterious impact on the overall equity market. Fortunately, these risks can be avoided and we continue to find very attractive combinations of quality and value such that the free cash flow yield on next-twelve-month consensus estimates relative to market cap for our U.S. Fundamental Stability & Value strategy is substantially above that of the S&P 500 and consistent with the yield that was available immediately following the financial crisis (see **Figure 1** below.)

Performance Summary

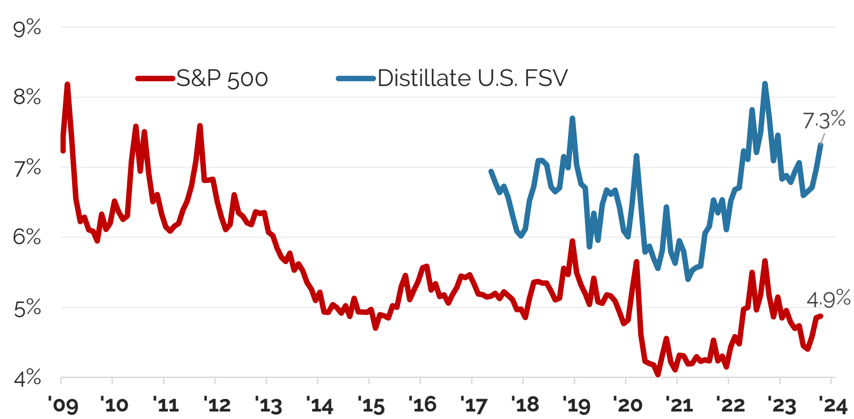
U.S. Fundamental Stability & Value (U.S. FSV): In the first three quarters of 2023, our U.S. large-cap strategy returned 10.43% after fees and lagged the S&P 500's 13.07% return by 2.64%. Performance of the S&P 500 this year is extremely concentrated with just six large stocks (NVIDIA, Microsoft, Tesla, Meta, Amazon, and Apple) contributing nearly 9.6% of the benchmark's 13.1% total return. These stocks appear richly valued on a free cash flow basis and increasingly so after their performance this year. Against the Russell 1000 Value ETF, our U.S. FSV strategy has outperformed by 8.74% year-to-date through Q3. Annualized net of fee returns remains solidly ahead of each benchmark since inception, at 2.38% and 6.85% above the S&P 500 Index and Russell 1000 Value ETF (See **Figure 2** on the following page).

U.S. Small/Mid Cap Quality & Value (SMID QV): Our SMID QV strategy outperformed the Russell 2000 benchmark by 12.47% and the Russell 2000 Value benchmark by 15.59% in the first three quarters of the year, and annualized excess returns since inception and net of fees are 10.26% and 10.05% ahead of those benchmarks (See **Figure 3** on the following page).

International Fundamental Stability & Value (Intl. FSV): Our International FSV strategy returned 9.26% after fees through Q3 2023, which was 4.25% ahead of the MSCI All Country Ex US ETF benchmark. Annualized net of fee performance since inception is ahead of its benchmark by 0.91% (See **Figure 4** on page 3).

U.S. Large Cap Value Long 130%/Short 30% (U.S. Value 130/30): Our 130/30 strategy returned 5.05% net of fees through 3Q 2023, trailing the 13.07% return of the S&P 500 Index. 3Q returns for the strategy were nearly 6% ahead of the S&P 500, and annualized net of fee returns remain ahead of the S&P 500 by 7.42% and above the Russell 1000 Value ETF by 11.96% (See **Figure 5** on page 3).

Figure 1: Free Cash to Mkt Cap Yield for the S&P 500 vs. Distillate's U.S. FSV



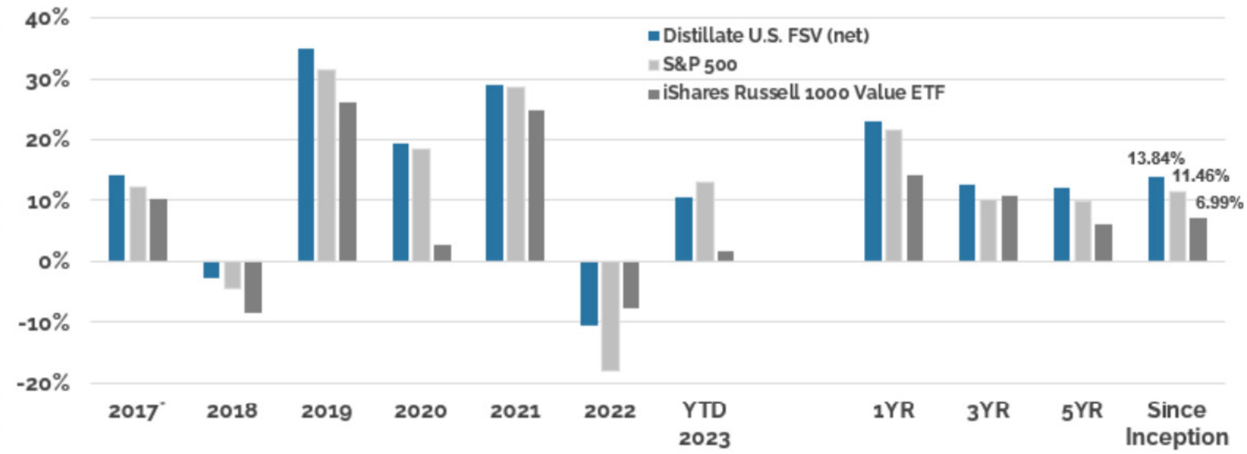
Source: FactSet

Performance Charts: **Figures 2 through 5** depict net returns for Distillate's U.S. FSV, SMID QV, International FSV and U.S. Value 130/30 composite strategies versus their respective benchmarks since inception.

Figure 2: Distillate U.S. Fundamental Stability & Value Composite Performance

As of September 30, 2023

	2017*	2018	2019	2020	2021	2022	YTD 2023	1YR	3YR	5YR	Since Inception
Distillate U.S. FSV (net)	14.18%	-2.79%	34.91%	19.22%	28.91%	-10.58%	10.43%	22.86%	12.63%	12.19%	13.84%
S&P 500	12.11%	-4.39%	31.49%	18.40%	28.71%	-18.11%	13.07%	21.62%	10.15%	9.91%	11.46%
iShares Russell 1000 Value ETF	10.27%	-8.41%	26.13%	2.73%	24.91%	-7.72%	1.69%	14.26%	10.87%	6.03%	6.99%

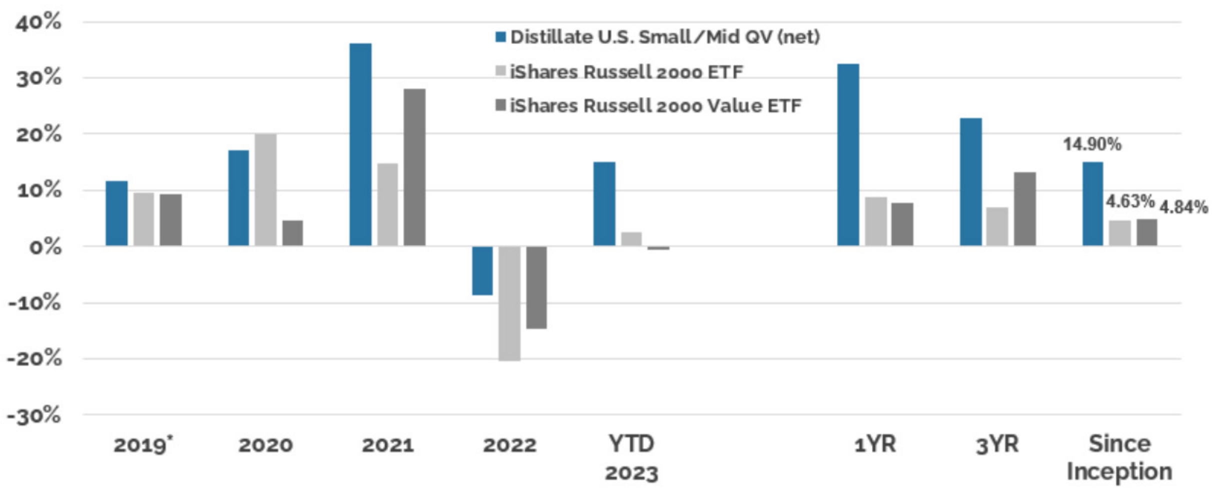


Source: U.S. Bank, Morningstar Data; Inception 5/31/2017; the period "2017*" reflects returns from inception through 12/31/2017. One cannot invest directly in an index. See performance disclosures.

Figure 3: Distillate U.S. Small/Mid Quality & Value Composite Performance

As of September 30, 2023

	2019*	2020	2021	2022	YTD 2023	1YR	3YR	5YR	Since Inception
Distillate U.S. Small/Mid QV (net)	11.65%	17.15%	36.03%	-8.64%	14.92%	32.41%	22.92%		14.90%
iShares Russell 2000 ETF	9.49%	19.91%	14.64%	-20.49%	2.45%	8.81%	7.05%		4.63%
iShares Russell 2000 Value ETF	9.18%	4.50%	27.96%	-14.67%	-0.68%	7.62%	13.07%		4.84%



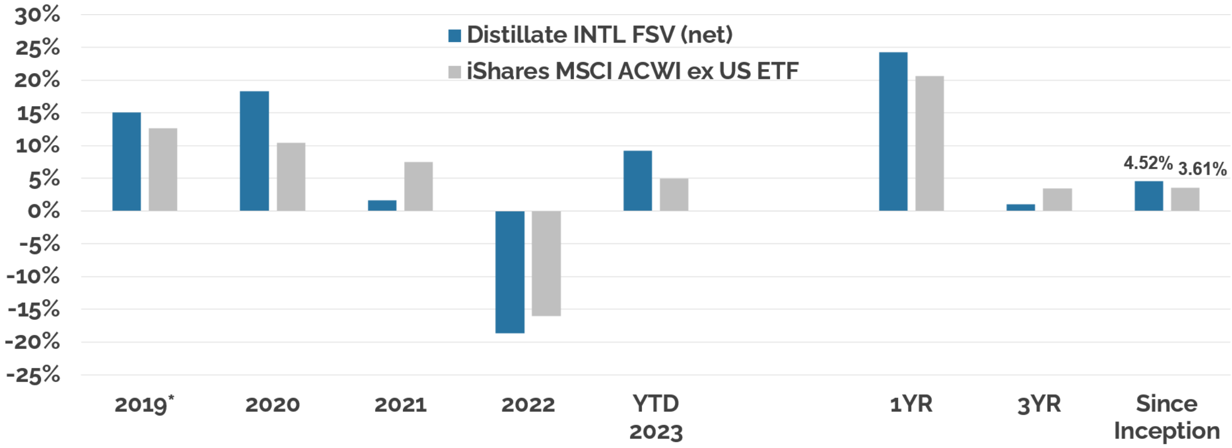
Source: U.S. Bank, Morningstar Data; Inception 3/31/2019; the period "2019*" reflects returns from inception through 12/31/2019. One cannot invest directly in an index. See performance disclosures.

Past performance does not guarantee future results. See disclosures.

Figure 4: Distillate INTL Fundamental Stability & Value Composite Performance

As of September 30, 2023

	2019*	2020	2021	2022	YTD 2023	1YR	3YR	5YR	Since Inception
Distillate INTL FSV (net)	15.08%	18.26%	1.67%	-18.68%	9.26%	24.22%	0.99%		4.52%
iShares MSCI ACWI ex US ETF	12.67%	10.48%	7.48%	-16.01%	5.01%	20.67%	3.50%		3.61%

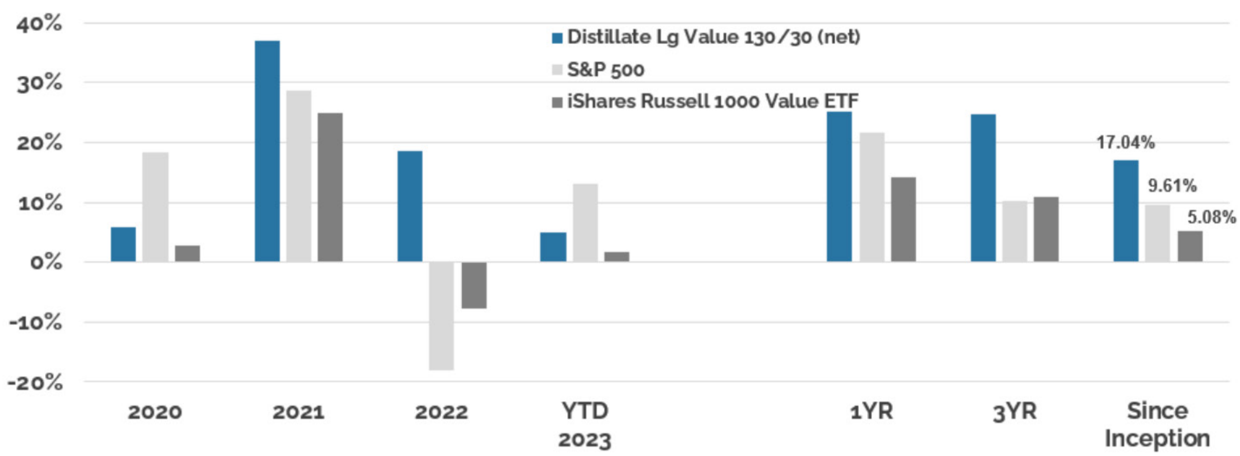


Source: U.S. Bank, Morningstar Data; Inception 1/31/2019; the period "2019*" reflects returns from inception through 12/31/2019. One cannot invest directly in an index. See performance disclosures.

Figure 5: Distillate U.S. Large Cap Value 130/30 Composite Performance

As of September 30, 2023

	2020	2021	2022	YTD 2023	1YR	3YR	5YR	Since Inception
Distillate Lg Value 130/30 (net)	5.81%	36.86%	18.59%	5.05%	25.11%	24.71%		17.04%
S&P 500	18.40%	28.71%	-18.11%	13.07%	21.62%	10.15%		9.61%
iShares Russell 1000 Value ETF	2.73%	24.91%	-7.72%	1.69%	14.26%	10.87%		5.08%



Source: U.S. Bank, Morningstar Data; Inception 12/31/2019. One cannot invest directly in an index. See performance disclosures.

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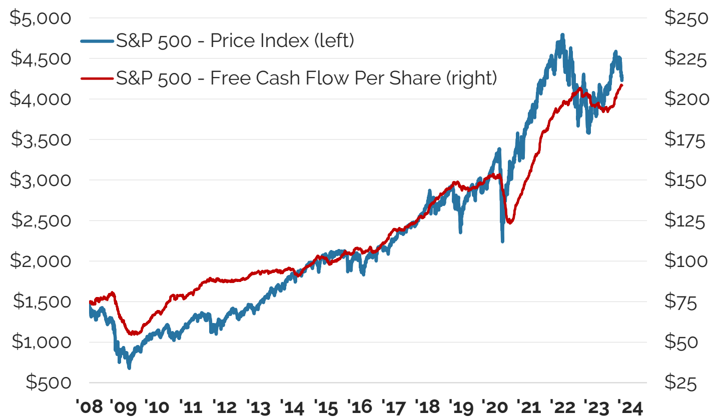
Market Commentary:

Amidst a varied macroeconomic backdrop that included banking turmoil at the start of the year, sluggishness abroad, and sharply higher interest rates, free cash flows for the S&P 500 Index have been resilient. Next-twelve-month (NTM) forward estimates have continued to plod higher after moderating from a peak in 2022. The S&P 500 Index price increased alongside these rising estimates until recently when concerns about higher interest rates seem to have overwhelmed the underlying improvement in fundamentals (See **Figure 6**).

Free cash estimates have moved higher and prices have followed suit until very recently when prices corrected as free cash kept rising.

Figure 6: S&P 500 Free Cash Flow vs. Price

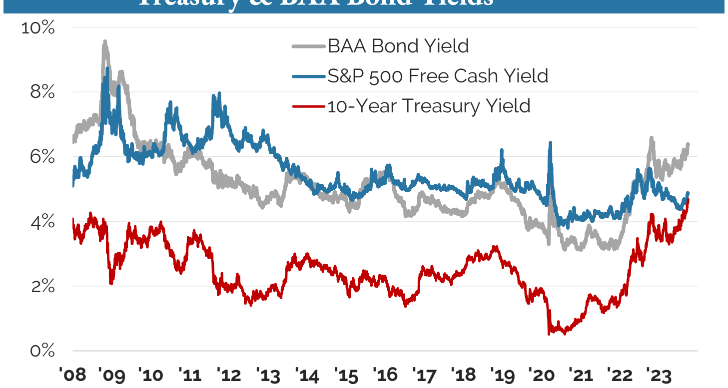


Source: FactSet, data as of 10/4/2023

This recent combination of rising free cash flow estimates and falling prices have caused the free cash flow (FCF) yield on the S&P 500 Index to return to the 5% level that prevailed for much of the prior decade. But at the same time that equity FCF yields have moved higher, 10-year Treasury and BAA-bond yields have risen even more. Consequently, equities look more expensive against bonds than they have in the recent past with a FCF yield that is now well below the BAA bond yield and only slightly ahead of the 10-year Treasury yield (See **Figure 7**).

Equity free cash yields are now in line with 10-year treasury yields and below BAA-bond yields.

Figure 7: Equity Free Cash Yield (NTM) vs. 10-Year Treasury & BAA Bond Yields

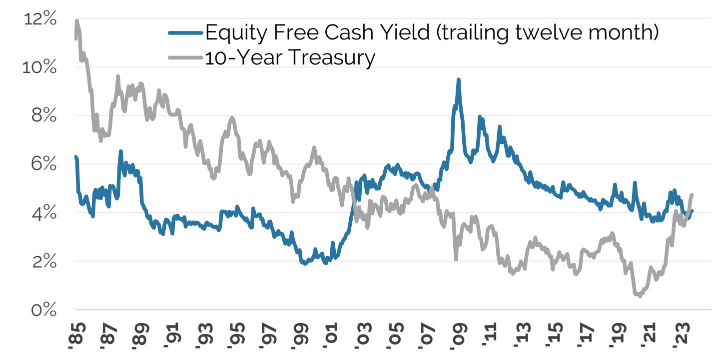


Source: FactSet, data as of 10/4/2023

While equities look expensive relative to bonds compared to their recent past, the longer-term history is more nuanced. Using trailing data for equity FCF yields in order to go back further in time, the relationship is less straight forward with equity FCF yields being significantly below 10-Year Treasury bond yields for much of the available history (See **Figure 8**). Intuitively, it makes sense that equities should trade at a lower yield than bonds since the free cash flows underpinning the equity yield grow (historically at 9% per year) while the bond payments are fixed. In that context, the recent period when equity FCF yields were higher looks anomalous in that equities offered both a higher starting yield and the benefit of growth. Equities during that period looked like the much more attractive option and in fact generated an over-500% return over the last 20 years compared to just 75% for the Barclays U.S. Aggregate bond index. At present, the relationship between equity FCF yields and bond yields looks more normal and there is a more reasonable trade-off for people who want a guaranteed fixed payment with less price variability and those who are willing to trade-off short-term price volatility for longer-term growth.

Equity free cash yields have traded at significant discounts to bond yields for much of the available history.

Figure 8: Historical S&P 500 Trailing Free Cash Yield vs. 10-Year Treasury Yields

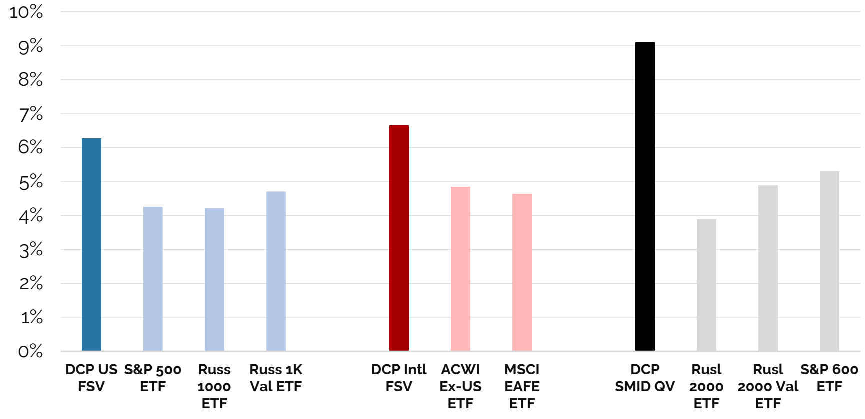


Source: FactSet, Standard & Poor's 10/4/2023

In the near-term, we do not know how investors will price the long-term advantage of equity free cash flow relative to fixed-income alternatives and what this will mean for equity prices. Over the longer-term, however, a 5% starting FCF yield on forward estimates that offers the benefits of growth and inflation protection does not seem unreasonable relative to current bond yields, either in a longer-term historical context or logically. Beneath this 5% figure, however, are a number of richly valued equities where this trade-off is less appealing and where there appears to be greater price risk. In a world of 5% risk-free bond yields, stocks with low single-digit FCF yields are implicitly pricing in substantial future growth. Given the enormous size of a number of these stocks, if some of them fail to meet lofty embedded growth expectations, they could impose a considerable drag on the overall S&P 500 benchmark. Outside of these stocks, however, there is significant opportunity, and it is from that pool that we are able to achieve a 7.3% free cash yield on our U.S. FSV strategy that compares even more favorably to current bond yields while also emphasizing quality and low financial leverage.

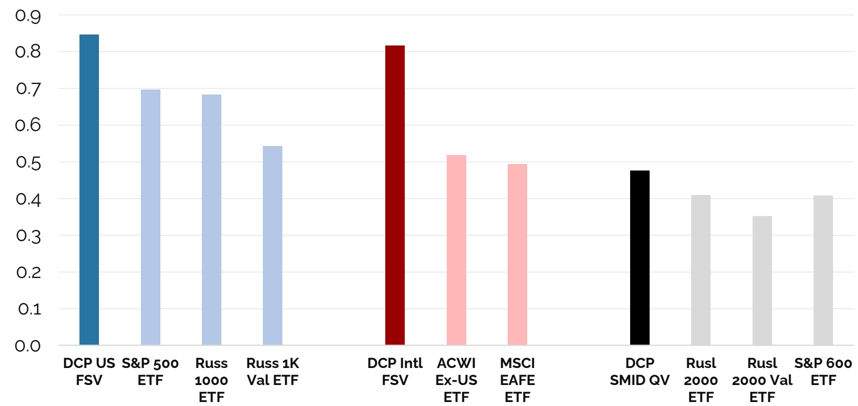
Valuation & Quality Statistics: Distillate's strategies offer attractive levels of free cash yield, cash flow stability, and balance sheet leverage.

Figure 9 (Valuation): Next 12-Month Free Cash Flow to Enterprise Value



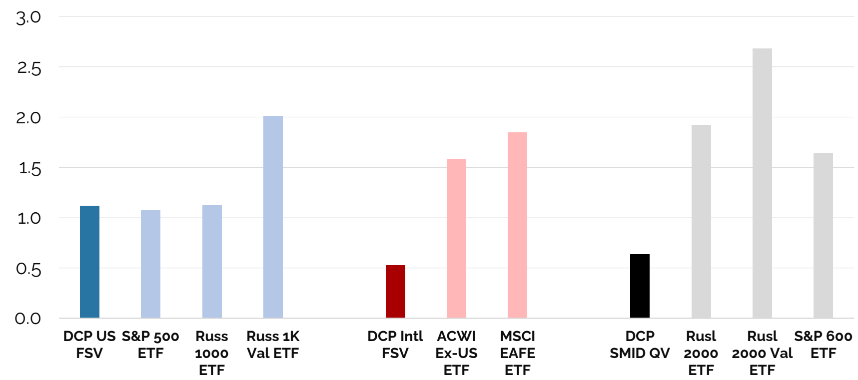
Source: FactSet, See end-notes for methodology. As 10/4/2023

Figure 10 (Quality): Distillate's Cash Flow Stability Score



Source: FactSet, See end-notes for methodology. As of 10/4/2023

Figure 11 (Quality): Net Debt to Adjusted EBITDA



Source: FactSet, See end-notes for methodology. As of 10/4/2023

Valuation & Quality vs. Indexes:

Figures 9-11 compare Distillate's strategies to their various benchmarks on valuation and quality. These figures highlight how our strategies are differentiated from the benchmarks where we see key risks in valuation for large-cap U.S. stocks; leverage among smaller U.S. stocks; and a combination of valuation, stability, and leverage generating avoidable risk internationally.

Figure 9 compares next-twelve-month estimated free cash flow to enterprise value, and highlights substantial valuation advantages for each of Distillate's strategies versus their relevant benchmarks. The FCF yield of the U.S. FSV strategy over the S&P 500 is at its widest point since inception and reflects the opportunity available by being selective and avoiding several large and expensive stocks that are depressing the overall market's attractiveness. Our international strategy is also highly differentiated versus its main benchmark which itself is more attractively valued than its U.S. counterpart after years of underperformance. The small/mid cap strategy also enjoys a significantly more attractive valuation than its benchmarks, where high leverage and a significant number of unprofitable firms are dampening valuations.

Figure 10 depicts the relative fundamental stability scores that we utilize in portfolio construction, with a higher score equating to greater stability. We believe the greater underlying fundamental stability of our strategies is particularly important to our goal of preserving capital in adverse economic scenarios, including recessions.

Figure 11 measures leverage in the form of total debt relative to normalized lease-adjusted consensus estimates for earnings before interest, taxation, depreciation, and amortization (EBITDA). Our preference always is to avoid highly levered situations, but amid rising interest rates and bond yields, we believe debt is a critical variable to examine in the context of protecting capital, and a key differentiator for our strategies currently. We have clearly seen the dangers of leverage playing out with regard to smaller U.S. banks this year, and in the small cap space, leverage is an even bigger issue as it is high among smaller cap companies despite the fact that the fundamentals for these companies are more volatile and they are thus on average less able to support higher debt burdens.

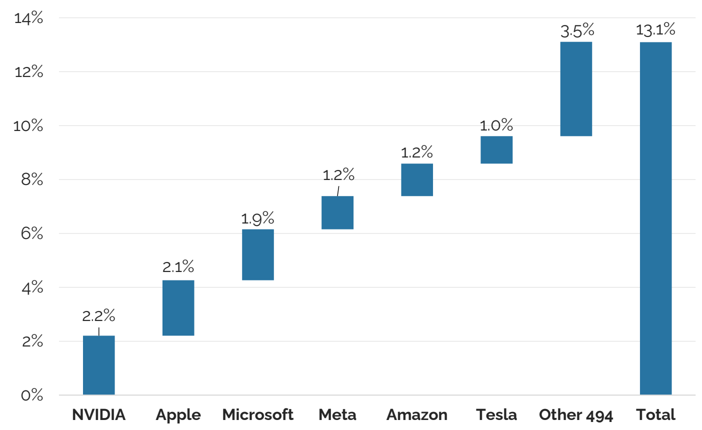
Performance:

U.S. Fundamental Stability & Value (U.S. FSV)

Distillate's U.S. FSV strategy returned 10.43% through Q3 2023 on a total return basis net of fees, compared to 13.07% for the S&P 500 benchmark. This year has seen an enormous headwind to performance from the very concentrated gains of just a few mega-cap stocks that are unowned due to their rich valuations. These six stocks collectively are responsible for 69% of the benchmark's aggregate 13.1% return (See **Figure 12**). Within our portfolio, Jabil Inc., Broadcom, and Owens Corning were the largest contributors to relative performance while Advanced Auto Parts, CVS, and PayPal were the biggest detractors.

Much of the S&P 500's gains through Q3 are due to only a few stocks.

Figure 12: S&P 500 Contribution to Return 2023 to Q3



Source:FactSet

U.S. Small/Mid Quality & Value (SMID QV)

Distillate's SMID QV strategy returned 14.92% on a total return net-of-fee basis through Q32023 compared to 2.45% and -0.68% for the Russell 2000 ETF and Russell 2000 Value ETF. The strategy's annualized performance is now 10.26% and 10.05% ahead of the same benchmarks since inception in 2019. Top contributors year-to-date include Builders FirstSource, Owens Corning, and AutoNation. The largest detractors from relative performance were Victoria's Secret Company, Super Micro Computer (unowned), and Advanced Auto Parts. Performance contributions were well balanced with the top 5 stocks contributing around 21% of the excess return versus the benchmarks.

International Fundamental Stability & Value (Intl. FSV)

Distillate's Intl. FSV strategy returned 9.26% net of fees in the first three quarters of 2023 and eclipsed the 5.01% return MSCI ACWI Ex-US benchmark by 4.25%. Among owned positions, strong contributors included Advantest, LVMH Moet Hennessy Louis Vuitton, and Industria de Diseno Textil. Relative performance was positive across almost all sectors and in all major regions.

As a reminder, region weights are limited to 150% of the benchmark weight to avoid the potential for any one region to have an outsized impact on performance, but weights are otherwise determined by bottom-up stock selection. The largest detractors from relative performance were NCsoft Corporation, Teleperformance, and Roche. Stronger performance this year is helping to offset underperformance in each of the last two years when an underweight to bank stocks created a meaningful headwind for our strategy. Aided also by strong relative gains in 2019 and 2020, annualized performance net of fees is 0.91% above the MSCI ACWI Ex-US benchmark since inception.

U.S. Large Cap Long 130/Short 30 (U.S. 130/30)

Our U.S. 130/30 strategy supplements our U.S. FSV strategy as a levered valuation-only strategy that is designed to benefit not only from buying the 100 cheapest names among the largest 500 U.S. stocks, but also from being short the most expensive 100 in that group. Being levered and without the same quality filters of our U.S. FSV, performance of U.S. 130/30 has been, and will likely continue to be, much more varied than its U.S. FSV counterpart. In the first three quarters of 2023, the strategy returned 5.05% net of fees which trailed the 13.07% gain of the S&P 500 Index. Similar to the headwind faced by the U.S. FSV strategy but without the benefit of owning Apple in the first quarter or Alphabet in each quarter, the strategy faced a significant headwind. The short side of the strategy lagged the market, but not by enough to offset the underperformance of the more heavily weighted long side. Lagging the benchmark year-to-date in 2023 comes on the heels of significant outperformance in each of the prior two years such that annualized net of fee performance since inception in 2020 is 7.42% ahead of the S&P 500 Index and 11.96% above that of the Russell 1000 Value ETF.

Changes & Valuation

U.S. Fundamental Stability & Value (U.S. FSV)

Distillate Capital's U.S. FSV Strategy is less expensive, more fundamentally stable, and less levered to the S&P 500.

Table 1: U.S. FSV Portfolio Characteristics*

	U.S. FSV	S&P 500
Free Cash Yield to Mkt Cap[1]	7.3%	4.9%
Free Cash Yield to EV[1]	6.3%	4.3%
P/E[2]	14.2	17.8
Leverage[3]	1.1	1.1
Fundamental Stability[4]	0.86	0.70

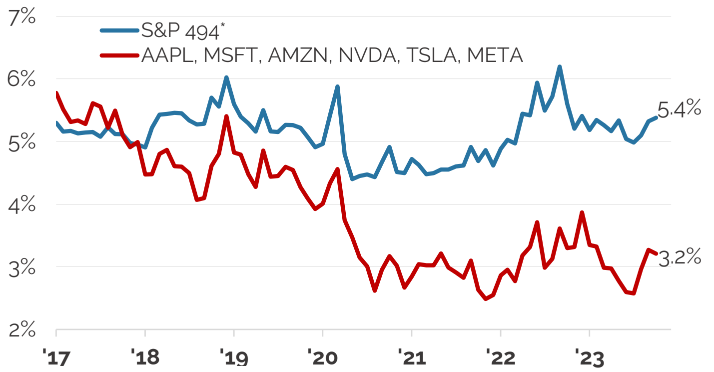
*as of 10/4/2023, see methodology endnotes.

After rebalancing, Distillate's U.S. FSV strategy's free cash flow to market cap yield valuation of 7.3% compares very favorably to the 4.9% offered by the S&P 500 benchmark. There remains a wide dispersion in valuations in the market and much commentary is now being made of "The Magnificent 7" and their overall impact on performance and valuation of the S&P 500. Our work focuses on six stocks rather than the typical list of seven. Apple, Amazon, Meta, Microsoft, NVIDIA, and Tesla are shown collectively in **Figure 13**, highlighting their valuation versus the valuation of the remaining 494 constituents of the S&P 500 over time. We are highlighting that group of six rather than Wall Street's "Magnificent 7" which includes Alphabet, as we believe Alphabet shares are not as expensive and the stock remains a position in U. S. FSV.

Looking back, while this group of six mega-cap stocks were at one point less expensive than the remainder of the market, they are now significantly more expensive, and given their large collective 24% weight in the index, are meaningfully impacting the overall market valuation. Expectations for growth embedded in valuations of that group of six are indeed high, and while some of that growth will likely be realized as they benefit from their exposure to AI, we see the risk/reward profile for those stocks as unfavorable and believe that in aggregate they create a substantial risk that is important to navigate around.

Several large expensive stocks are pulling down the overall market's yield; the valuation outside of these stocks is much more appealing.

Figure 13: Free Cash to Mkt Cap Yield for the Expensive Megacap 6 and Remaining S&P 494



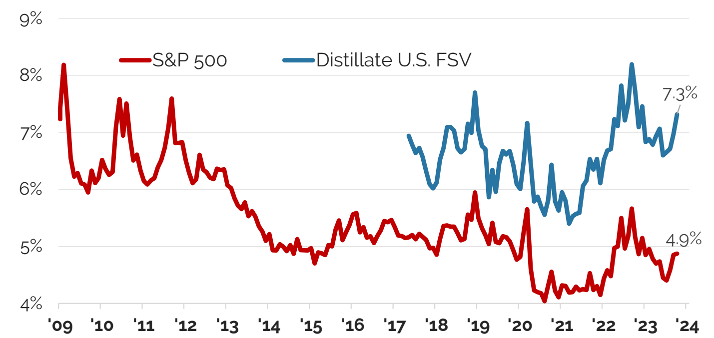
Source: FactSet

Avoiding those six and other expensive stocks and focusing on the segments of the market where quality and valuation overlap, we are able to assemble a portfolio that is significantly more attractively valued than the overall benchmark while at the same time having leverage and stability characteristics that we believe are critical to long-term capital preservation.

The 2.4% FCF yield spread of our U.S. FSV strategy over that of the S&P 500 is near an all-time high, and the absolute valuation of Distillate's U.S. FSV strategy is now near a level consistent with that of the S&P 500 during the aftermath of the great financial crisis in the late 2000's and early 2010's (see **Figure 14**).

Several large expensive stocks are pulling down the overall market's yield; the valuation outside of these stocks if much more appealing.

Figure 14: Free Cash to Mkt Cap Yield for the S&P 500 vs. Distillate's U.S. FSV Strategy



Source: FactSet

Sector Changes: As a reminder, there is no top-down sector constraint on our strategies as portfolio construction is driven by bottom-up stock selection. Within that framework, the largest sector change in the recently completed rebalance was a 3-percentage point reduction in health care that was offset by a comparable increase in industrials. These changes mirror recent performance where health care modestly outperformed last quarter and industrials lagged the market. Current sector weights relative to the S&P 500 are shown in **Table 2** which also breaks out the distortive impact of several mega-cap stocks in certain sectors for better comparison.

Sector weights are driven by bottom-up stock selection.

Table 2: U.S. FSV Sector Exposure*

	U.S. FSV	S&P 500
Communication Services	9.8%	9.1%
Consumer Discretionary	11.4%	10.5%
Ex AMZN & TSLA	*11.4%*	*5.1%*
Consumer Staples	6.8%	6.5%
Energy	2.3%	4.5%
Financials	9.3%	12.5%
Ex Banks	*9.3%*	*8.8%*
Health Care	20.8%	13.4%
Industrials	20.6%	8.3%
Information Technology	16.8%	28.0%
Ex Apple & Microsoft	*16.8%*	*14.1%*
Materials	1.5%	2.5%
Real Estate	0.8%	2.3%
Utilities	0.0%	2.3%

*as of 10/4/2023

Sells: The largest exited positions in the quarter were Danaher, Aon, and Avery Denison. Danaher and Avery Denison outperformed the broader market in the last quarter and the positions were exited as their valuations became stretched beyond the threshold for inclusion. Avery Denison slightly lagged the market but was also sold on valuation as its free cash estimates have deteriorated recently.

Buys: The largest new purchases were Ameriprise, Paccar, and CSX. Each stock looks attractively valued relative to the broader benchmark and also offers an attractive combination of cash flow stability and low leverage.

Adds/Trims: The largest additions to existing positions were Etsy and Omnicom, which both rose in weight after underperforming by around 20 percentage points last quarter such that their valuations have become substantially more attractive. Amgen and Alphabet were the largest trims after outperforming by around 25% and 12% in the quarter, respectively.

U.S. Small/Mid Cap Quality & Value (SMID QV)

There is enormous range of valuations in the small and mid-cap space and those valuations can look wildly different depending on whether leverage is included and how unprofitable stocks are considered. Unprofitable stocks make up a large share of the most popular small cap benchmarks but we often see them excluded from P/E calculations when statements about small cap valuations are being made. Looking more granularly and utilizing FCF yields that we believe provide a much fairer and debt-inclusive view of the opportunities, we find that selectivity in the space allows us to build portfolios that stand out significantly from the benchmarks. Distillate's small/mid cap strategy of 150 stocks offers a very attractive 9.1% free cash flow to enterprise value yield that is more than double that of the Russell 2000 ETF, and 4.2% above that of the Russell 2000 Value ETF (See **Table 3**).

Our Small/Mid Cap strategy is also highly differentiated in terms of indebtedness, a key issue we wrote about in a recent white paper "Small Stocks Big Debt Problems." Leverage is very elevated among small cap stocks and is likely to be a significant issue as maturing debt must be rolled in a market where interest rates and thus borrowing costs have moved meaningfully higher. Distillate's strategy avoids this by limiting debt, and after rebalancing, the portfolio has a leverage ratio of 0.6x versus 1.9x and 2.7x for the Russell 2000 and Russell 2000 Value benchmarks (See **Table 3**).

Lastly and also related to quality, Distillate's SMID QV has no positions in stocks that have negative next-twelve-month free cash flow estimates. For the Russell 2000 and Russell 2000 Value benchmarks, 14% of each benchmark consists of equities that are not expected to earn positive free cash flow in the next twelve months. For the S&P 500, by way of comparison, this figure is 3%. Combined with financial leverage and an unknown economic environment, we believe selectivity in small and mid-caps is especially important.

The largest new purchases, Interpublic Group and LKQ, are consistent with the criteria outlined above and offer 11% and 8% FCF yields, respectively. The biggest sales, CF Industries and Marathon Oil, outperformed by 30% and 25% respectively and no longer fit the size criteria for inclusion.

Distillate's U.S. Small/Mid Cap Quality & Value strategy is more attractively valued and less indebted than its benchmarks

Table 3: U.S. Small/Mid Cap QV Characteristics*

	SMID QV	Russell 2000 ETF	Russell 2000 Value ETF
Free Cash Yield to Mkt Cap[1]	11.5%	5.5%	7.3%
Free Cash Yield to EV[1]	9.1%	3.9%	4.9%
P/E[2]	8.7	12.1	9.9
Leverage[3]	0.6	1.9	2.7
Fundamental Stability[4]	0.48	0.41	0.35
Negative FCF Weight[5]	0.0%	14%	14%

*as of 10/4/2023, see methodology endnotes.

International Fundamental Stability & Value (Intl. FSV)

After rebalancing, Distillate's International FSV strategy offers a higher free cash flow yield both to market cap and enterprise value, and has substantially more-stable fundamentals and less leverage than the index (See **Table 4**). The international FSV strategy is thus significantly differentiated from its benchmark not just on valuation, but critically on quality as well.

Distillate Capital's International FSV Strategy is less expensive, more fundamentally stable, and less levered than its benchmark.

Table 4: International FSV Portfolio Characteristics*

	Intl. FSV	ACWI Ex-US
Free Cash Yield to Mkt Cap[1]	7.4%	5.9%
Free Cash Yield to EV[1]	6.7%	4.8%
P/E[2]	13.1	11.8
Leverage[3]	0.5	1.6
Fundamental Stability[4]	0.82	0.52

*as of 10/4/2023, see methodology endnotes.

Changes & Regional Weights: The largest purchase in the quarter was LVMH, which lagged the MSCI ACWI Ex-US Index by approximate 15% last quarter and now offers an attractive 5.1% FCF yield on a business that rapidly and consistently grows its free cash flows and has low leverage. The largest sold position was Samsung Electronics which has seen its estimated free cash flows fall precipitously on plans for massive capital outlays. The biggest increased existing position was Alibaba, which has seen its valuation improve markedly to a nearly 13% free cash flow to enterprise value yield. The biggest trim was Prio which was reduced after outperforming the benchmark by around 30% last quarter.

Regional weights after the quarterly rebalance remain fairly well matched with the ACWI Ex-U.S. benchmark. Japan is the largest overweight at 20% vs. 14.5% for the benchmark. There are key differences under the surface in some regions. As an example, our China weight consisting largely of technology and retail whereas banks, developers and other financial firms make up a large share in the benchmark. (See **Table 5**).

Regional weights reflect bottom-up stock selection but are limited to 150% of the region benchmark weight to limit geographic concentration risk.

Table 5: International FSV Portfolio Characteristics*

	Intl. FSV	ACWI Ex-US
Europe	44.4%	42.6%
Japan	20.0%	14.5%
Asia Ex China & Japan	12.2%	19.7%
China & Hong Kong	9.2%	9.6%
Americas	14.2%	10.0%
Middle East & Africa	0.0%	3.6%

*as of 10/4/2023 based on FactSet headquarters definition.

U.S. Large Cap Long 130/Short 30 (U.S. 130/30)

The overall goal of the 130/30 strategy were outlined in the performance section, but are also evident in the portfolio characteristics which show a wide divergence between the valuation of the long and short portfolios (See **Table 6**).

Distillate's 130/30 strategy seeks to capitalize on valuation divergences in the market which remain wide as evidenced by the large gap between the valuations available on the long and short portfolios.

Table 6: U.S. 130/30 Characteristics*

	Long	Short	S&P 500
Free Cash Yield to Mkt Cap[1]	10.3%	0.2%	4.9%
Free Cash Yield to EV[1]	8.1%	0.2%	4.3%
P/E[2]	10.1	20.8	17.8
Leverage[3]	1.3	2.1	1.1
Fundamental Stability[4]	0.59	0.53	0.70
Negative FCF Weight[5]	0%	35%	3%

*as of 10/4/2023, see methodology endnotes.

Final Word

History tell us that trends such as the current "Magnificent Seven" have an ability to run on and push equity prices well past the points where you might expect them to stop. Moments of pressure also very typically create opportunities that are larger than logic (and a lot of academic theory) would suggest. And there are times when headlines mask both opportunities and risks below the surface. Thus the market creates opportunities for those with a long-term view and discipline.

In large caps, as we noted, the absolute FCF yield on our U.S. FSV strategy now stands at a level comparable to that of the S&P 500 at the end of the great financial crisis, a time when investing in equities ultimately proved to be very rewarding. Yet we also note the current level of concentration in the market and stretched valuations on that same group of stocks. Should the high levels of growth implicit in those rich valuations fail to materialize for even some portion of those stocks, given their size, resulting price underperformance could impose a meaningful drag on the overall market. As we have learned many times over in our careers, equity investing is not about what unfolds for a company but about what occurs relative to what was already priced into their shares. To us, the large weight and lofty expectations for a number of these stocks looks like a critical risk that we are happy to circumvent.

In small caps, there are two key risks. First, there is a mirage of attractiveness in that P/E ratios that are cited as indicating low valuations for common benchmarks typically exclude unprofitable companies that constitute a large percentage of the universe. If free cash flow measures are instead used and unprofitable companies are included, relative valuations for small cap stocks overall look very different and not nearly as appealing. Second, there is a significant debt issue to be dealt with in that segment of the market. Leverage is high and interest costs that are already eating into profits are likely to increase substantially as lower cost debt issued in years past is replaced over time with higher cost debt that reflects the current interest rate environment. Aside from these two issues, however, there are a large number of stocks that are very attractively valued and have little debt and our Small/Mid QV strategy reflects this. We believe there is significant value in being selective.

While these valuation and debt issues look to be key hazards to avoid, we very much do not want to join the noise of pundits and prognosticators who confidently declare how and when such perceived risks will play out. Instead of having to decide whether, how, and when a risk will resolve itself, we believe diversified strategies of less expensive, more fundamentally stable, and less leveraged stocks will be resilient over the longer-term to both the risks we are able to identify, like some of those at present, as well as the ones we cannot, like the recent pandemic.

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The U.S. Dollar is the currency used to express performance. Returns are presented net of management fees and include the reinvestment of all income. For non-fee-paying accounts, net of fee performance was calculated using a modeled management fee equal to the highest investment management fee that may be charged for the applicable composite (see fee schedule below). For accounts calculated with a per share, net-of fee NAV, gross performance was calculated by adding back the unitary fee associated with that fund. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

The investment management fee schedule for the strategies discussed are as follows: 0.39% for U.S. Fundamental Stability & Value; 0.55% for U.S. Small/Mid Quality & Value; 0.79% for U.S. Large Cap Value 130/30; and 0.55% for International Fundamental Stability & Value. Management fees may vary and are negotiable.

Data for the Firm's investment strategies are based on a representative account for each composite. Actual holdings and performance may differ between accounts or vehicles offered by the Firm due to the size of an account, client guidelines, or other constraints and restrictions related to that account or vehicle.

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This presentation contains forward looking statements, which can be identified by the use of forward-looking terminology such as "may", "will", "should", "expect", "anticipate", "target", "project"," estimate", "intend", or "believe", or the negatives thereof or any other variations thereon or other comparable terminology. Because such forward looking statements involve risk and uncertainties, actual results may differ materially from such expectations or projections. Any such forward-looking statements should not be construed to be indicative of the actual events that will occur nor should they be considered guarantees of future events in any form.

The ***U.S. Fundamental Stability & Value*** *composite seeks to distill a starting universe of large cap U.S. equities into only the stocks where quality and value overlap using Distillate's proprietary definitions. Its goal is to achieve superior compounded long-term returns by limiting downside in periods of market stress, while still providing strong performance in up markets. This composite was created in May 2017.*

The ***U.S. Small/Mid Cap Quality & Value*** *composite seeks to distill a starting universe of small- and mid-cap U.S. equities into only the stocks where quality and value overlap using Distillate's proprietary definitions. Its goal is to achieve superior compounded long-term returns by limiting downside in periods of market stress, while still providing strong performance in up markets. This composite was created in March 2019.*

The ***International Fundamental Stability & Value*** *composite seeks to distill a starting universe of large- and mid-cap non-U.S. equities into only the stocks where quality and value overlap using Distillate's proprietary definitions. Its goal is to achieve superior compounded long-term returns by limiting downside in periods of market stress, while still providing strong performance in up markets. This composite was created in January 2019.*

The ***U.S. Large Cap Value 130/30*** *composite seeks long-term capital appreciation by holding approximately 130% of an account's value in the most attractively valued large cap U.S. stocks measured using Distillate's proprietary free cash flow valuation method. The market exposure in this composite is brought back to approximately 100% by selling short 30% of an account's value of the least attractively valued stocks among the same starting set. This composite was created in December 2019.*

Free Cash Flow *refers to a company's operating cash flow, less its capital expenditures.* ***Enterprise Value*** *refers to a company's market capitalization plus its net debt balance.* ***Free Cash Flow to Enterprise Value Yield*** *refers to a company's or group of companies' free cash flow divided by the company's (or companies') Enterprise Value, with a higher resulting ratio indicating a more attractive valuation. This metric is a valuation measure and not a form of investor yield.* ***Normalized Free Cash Yield (or Distilled Cash Yield)*** *refers to the firm's proprietary valuation measure that looks at estimated, adjusted free cash flow relative to a company's adjusted enterprise value. References to historical stocks that ranked well using this methodology refer only to these stocks' historical valuation and not their inclusion in any actual or hypothetical strategies/accounts managed by Distillate Capital Partners LLC. This metric is a valuation measure and not a form of investor yield.* ***Long-term Fundamental Stability*** *is Distillate Capital's proprietary measure of through-cycle cash flow stability with a higher value indicating greater stability.*

Methodology note for ***Figure 9****: free cash flow (FCF) figures reflect consensus estimates of next-twelve-months (NTM) FCF in comparison to enterprise value (EV) for the relevant portfolio/strategy or benchmark. Stocks without data are excluded and portfolios are reweighted accordingly. Stocks with FCF/EV* *values of greater than 50% or less than -20% have been eliminated to avoid distorting overall averages.*

*Methodology Notes for **Portfolio Characteristics Tables**: [1]**Free Cash Yield to Market Cap and Enterprise Value (EV)** are based on the next-twelve-month free cash flow estimates relative to market capitalization and EV, which adds Distillate's proprietary measure of indebtedness. Stocks without estimates in the are excluded and the remaining names are reweighted based on those exclusions. [2]**P/E** is based on consensus estimates for next-twelve-months and excludes P/Es over 250 and under 0 to avoid the distortion from outliers. [3]**Leverage** is based on Distillate Capital's proprietary measure of indebtedness which looks at the ratio of adjusted net debt to an adjusted measure of forecast Earnings Before Interest, Taxation, Depreciation, and Amortization (EBITDA.) [4]**Fundamental stability** is Distillate Capital's proprietary measure of through-cycle cash flow stability with a higher value indicating greater stability. [5]**Negative FCF weight** is measured as the weight of stocks with negative free cash estimate as a share of those with any estimate.*

*The **S&P 500 Index** is an index of roughly the largest 500 U.S. listed stocks maintained by Standard & Poor's. The **iShares Russell 1000 Value ETF** is an investable benchmark used as a proxy for its underlying index, the **Russell 1000 Value Index**, an index of U.S. listed stocks that possess attractive valuation as measured by FTSE Russell. The **iShares MSCI ACWI Ex-US ETF** is an investable benchmark used as a proxy for its underlying index, the **MSCI ACWI ex USA Index**, an index managed by MSCI representing large and mid cap stocks outside of the U.S. The **iShares Russell 2000 ETF** and **iShares Russell 2000 Value ETF** are investable benchmarks used as a proxies for the underlying indexes of the **Russell 2000 Index** (an index of U.S. listed small cap stocks) and the **Russell 2000 Value Index** (an index of U.S. listed small cap stocks that possess attractive valuation as measured FTSE Russell).*

Indices are not available for direct investment. Investment in a security or strategy designed to replicate the performance of an index will incur expenses, such as management fees and transaction costs, which would reduce returns.