Mawer U.S. Mid Cap Equity Fund, Series A

Q1 2023 | Performance Commentary

Market overview

Equity markets delivered positive returns in the first quarter building on the rally that began in the fourth quarter of last year. Inflation, while still high, has continued to show signs of easing, providing hope that the U.S. Federal Reserve and other central banks may not need to be as aggressive as feared in tightening monetary policy. At the same time, corporate earnings have been quite resilient and economic data better-than-feared, increasing optimism that a pronounced recession, or hard landing, may be avoided. An added wrinkle to the backdrop for macroeconomic prognosticators were the failures of or severe distress experienced by several U.S. and European banks which dampened equity sentiment late in the quarter and gave an additional reason for central banks to be more cautious on further monetary tightening.

In this environment, the best performing sectors in the Russell Mid Cap Index were those that saw the greatest drawdowns in 2022: communication services, growth-leaning IT, consumer discretionary, and Industrials. Energy stocks pulled back in sympathy with the price of oil, and the Financials sector was dragged down by its heavy weight in regional banks.

Performance commentary

The portfolio outperformed its benchmark by a fair margin during the first quarter of 2023.The biggest reason for the relative outperformance was superior stock selection in the financials sector. While the index was dragged down by a heavy weighting in banks, the portfolio had exposure to a plethora of financial services firms which collectively rose double-digits, led by Focus Financial Partners, which was up materially in the quarter on the back of an announced takeover offer. Strong security selection in the consumer discretionary sector, where top weight quality used goods retailer Winmark Corporation rose strongly, and no exposure to the disappointing energy sector were also contributors. Somewhat offsetting these factors were some weaker selections in the health care and information technology sectors—four of five health care holdings fell in the quarter, and the relatively smaller weighting in higher-growth technology stocks caused the companies we do hold in the portfolio to lag the index's strong sector return.

Looking ahead

As the recent bank failures illustrate, the historic rise in interest rates over the past year has the potential to cause unanticipated impacts on some companies, and it is possible that more impacts will be seen. However, the underlying vulnerability we are most concerned about is that certain businesses became overly reliant on steadily rising asset prices and easy access to cheap capital during the preceding era of artificially low rates. We are skeptical of businesses with high degrees of leverage for this very reason, but there are plenty of other general categories of vulnerabilities:

- Unprofitable companies that rely on continued access to capital markets to fund their operations
- Businesses whose very existence depends heavily on the government's will to allow them to operate
- Enterprises that produce negative externalities for the environment or the communities in which they operate
- Companies whose stock prices provide no margin of safety.

With uncertainty as to the path forward and given significant lags between policy implementation and the impact in the real economy, there are bound to be other unanticipated surprises on the horizon.
To be sure, there are scenarios in which investments in any company can return a total loss; even the strongest businesses have vulnerabilities that can be exposed by the right trigger and that is the risk we bear as equity investors. However, we are not paid as managers to avoid risks entirely, but rather to manage and

take on risks only with the appropriate return potential. This is why we employ a non-predictive decision-making approach that focuses on steering away from areas where those vulnerabilities are sharpest as opposed to forecasting specific events. As such, we use a probabilistic Monte Carlo valuation process to determine where we feel the rewards are commensurate with the risks taken. This requires a disciplined investment process, a culture in which different points of view are celebrated, and appropriate diversification that builds natural contradictions into the portfolio. And even though this "boring" approach may sacrifice possible short-term gains in certain market environments, we believe it should lead to better and more consistent outcomes over time.

Performance summary[1] (%)

As of March 31, 2023:

	YTD	3 Mo.	1 Yr.	3 Yrs.	5 Yrs.	10 Yrs.	Since Inception[2]
FUND	7.1	7.1	4.5	-	-	-	(3.6)
BENCHMARK	3.9	3.9	(1.2)	-	-	-	(3.3)

Calendar Year, as of December 31:

	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013
FUND	(14.5)	-	-	-	-	-	-	-	-	-
BENCHMARK	(11.3)	-	-	-	-	-	-	-	-	-

[1]Performance figures are net of management fees and operating expenses. Periods greater than one year are annualized. Performance figures are in Canadian dollar terms.
[2]Mawer U.S. Mid Cap Equity Fund Series A Inception: September 27, 2021.

Selections from Mawer's Art of Boring blog and podcast:

The Case for Non-Predictive Decision Making
How do investors figure out what a company is worth? (Especially in a higher inflationary and interest rate environment?)

Inflation's one-two punch
It's inflation's second punch that can deliver a blow that investors may not be expecting.

Post-Mortem: Learnings from 2022 | EP128
Chief Investment Officer Paul Moroz shares takeaways from the Research team's annual post-mortem discussions.

Disclaimer

Opinions and Forecasts:

This report includes certain statements that are "forward looking statements". All statements, other than statements of historical fact, included in this report that address activities, events or developments that the portfolio advisor, Mawer Investment Management Ltd., expects or anticipates will or may occur in the future, including such things as anticipated financial performance, are forward looking statements. The words "may", "could", "would", "should", "believe", "plan", "anticipate", "expect", "intend", "forecast", "objective" and similar expressions are intended to identify forward looking statements. These forward looking statements are subject to various risks and uncertainties, including the risks described in the Simplified Prospectus of the Fund, uncertainties and assumptions about the Fund, capital markets and economic factors, which could cause actual financial performance and expectations to differ materially from the anticipated performance or other expectations expressed. Economic factors include, but are not limited to, general economic, political and market factors in North America and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological change, changes in government regulations, unexpected judicial or regulatory proceedings, and catastrophic events.

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Benchmarks:

FUND	BENCHMARK
Mawer U.S. Mid Cap Equity Fund	Russell Midcap Index (TR)

Performance Disclosure and Requirements:

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the fund facts and the prospectus before investing. The indicated rates of return are the historical annual compounded total returns including changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. Mawer Funds are managed by Mawer Investment Management Ltd.

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