FAIRPOINTE CAPITAL

FAIRPOINTE MID-CAP STRATEGY

3RD QUARTER COMMENTARY 2020

Market Overview and Performance

On the heels of the second quarter's increases, equity markets continued to generate strong gains in the third quarter, driven by better than expected earnings results, a recovering job market, and accommodative fiscal policy. Large caps and technology stocks led the advance in the quarter and year to date. Fairpointe's Mid-Cap Strategy returned 5.6% (net of fees), topping the 4.8% return for the S&P 400 Index.

Top and Bottom Contributors

The top contributors to performance were Varian Medical Systems, Corning, Cars.com, Mattel, and Lions Gate Entertainment Corporation.

Varian Medical Systems is a global leader in radiation therapy with an installed base of over 8,500 linear accelerators. In August, Siemens Healthineers offered to acquire the company for $16.4 billion ($177.50 per share) in an all-cash deal at a 24% premium. The transaction is expected to close in the first half of 2021. This is a good example of why the portfolio has averaged 1.8 takeovers per year since inception. Varian is a market leader with a strong competitive position and a balance sheet that is attractive to a strategic acquiror. This was the portfolio's second takeover this year.

Corning is a world leader in material science for communication networks, electronics, healthcare, and automotive markets. Demand for the company's Gorilla Glass technology has exceeded expectations, and an improving auto market has driven demand for its emissions technology. We like the company's long-term growth prospects, which are driven by internet traffic, increasing screen sizes, and pollution control regulations.

Cars.com is a leading digital marketplace for automotive dealers and shoppers. Results exceeded expectations in the quarter due to cost control and revenue gains. We expect future results to benefit from the rollout of over 700 General Motors dealer websites and a recovery in automotive sales.

The detractors to performance were Scholastic Corporation, Hexcel Corporation, Adtalem Global Education, Nokia Oyj, and Meredith Corporation. Nokia declined less than 10%, and we continue to build the position.

Scholastic is a leading publisher of children's books. The company has been hurt by near-term, COVID-related school disruptions. We expect earnings to improve due to upcoming releases, including a new book from JK Rowling, and the eventual reopening of schools for in-person learning, post-COVID. The company maintains a strong balance sheet with net cash equal to 15% of its market cap. We added to the position in the quarter.

Hexcel holds the number one position in carbon fiber composites for the aerospace, defense, and wind energy markets. Carbon fiber is lighter and stronger than aluminum and helps customers achieve energy efficiency targets. All three markets offer secular growth and increasing content per application over an economic cycle. The commercial aerospace business accounts for more than 60% of the company's revenue, and demand is depressed in the near term due to COVID. The company remains profitable due to effective cost management and demand in the defense and wind energy markets. Hexcel's competitive position is intact, and the company retains a strong balance sheet to withstand the pandemic. We added to the position**.**

Adtalem has transformed its business under CEO Lisa Wardell. The company exited its DeVry University unit and sold its Brazil operations over the past two years. The company is now focused on healthcare education, which accounts for over 80% of its revenue. In the quarter, Adtalem announced its intent to acquire Walden, a healthcare-focused university that is 100% online. The transaction is expected to close in the middle of next year and to boost cash flow in the first year. We added to the position in the quarter.

Portfolio Changes

Fairpointe had an active quarter, adding one position and eliminating two. We initiated a position in **ResMed**, a stock that had been on our watch-list for some time. ResMed is a market leader in digital health technologies and cloud-connected medical devices that care for people with sleep apnea, chronic obstructive pulmonary disease (COPD), and other chronic diseases. The company has an installed base of more than 12 million devices that help improve patient lives and lower healthcare costs for chronic illnesses. ResMed has a strong balance sheet and generates greater than 20% net profit margins and return on equity (ROE). Sleep apnea remains an under-diagnosed condition that we expect to drive future growth. We eliminated **Domtar**, a producer of paper, packaging, and personal care products. The company announced its intention to explore strategic alternatives for its personal care business, which drove the stock price near fair value. We exited **Patterson Companies**, a distributor of dental and animal health supplies, due to its uncertain outlook and near-term fair valuation.

Portfolio Outlook and Observations

Bank of America recently reported that the past ten years have been even worse for value than the dot-com bubble. The combination of low inflation and slow GDP growth has caused investors to favor growth and increasingly crowd into large cap technology stocks. No one can say when the current technology dominance will end, but we see warning signs in the initial public offering (IPO) market. According to Dealogic, this year is shaping up to be the busiest year for IPOs since the tech bubble. In September, data warehousing company Snowflake issued shares at $120 per share. It now trades at $240 per share, is valued at 76x revenue, and is unprofitable. This continues last year’s trend, when only 24% of IPOs were completed by profitable companies according to Goldman Sachs.

Looking ahead to the fourth quarter, the only certainty for investors is uncertainty. The US election is fast approaching, and it is not clear the winner will be known on election night due to high demand for mail-in ballots. COVID continues to spread as we head into the flu season. At the same time, there are indications a COVID vaccine could be approved as early as late 2020. The potential for short-term volatility remains high and offers opportunity for long-term investors. We continue to increase our exposure to companies with higher growth prospects and returns on equity (ROE), while retaining a focus on valuation. As we have written previously, we have improved the portfolio’s quality factors, like growth and ROE, and reduced debt leverage over the past 18 months.

Thank you for your support and stay safe!

Fairpointe Investment Team

DISCLOSURE

Year End	Total Firm Assets (USD) (millions)	Composite Assets (USD) (millions)	Composite Number of Accounts	Annual Performance Results Composite Gross	Net	S&P MidCap	Russell MidCap	Composite Dispersion
2019	1,347	1,198	Five or Fewer	17.15%	16.36%	26.20%	30.54%	N.A.
2018	2,935	2,755	Eight	(17.62%)	(18.25%)	(11.08%)	(9.06%)	0.24%
2017	5,415	5,091	Seven	12.87%	12.01%	16.24%	18.52%	0.27%
2016	5,178	4,844	Eight	25.56%	24.59%	20.74%	13.80%	0.41%
2015	5,607	5,308	Eight	(9.74%)	(10.42%)	(2.18%)	(2.44%)	0.81%
2014	7,733	7,389	Seven	10.79%	9.97%	9.77%	13.22%	0.38%
2013	6,999	6,692	Seven	45.67%	44.58%	33.50%	34.76%	1.00%
2012	3,853	3,633	Six	17.76%	16.83%	17.88%	17.28%	N.A.
2011	3,398	3,210	Five or Fewer	(5.36%)	(6.10%)	(1.73%)	(1.55%)	N.A.
2010*	-	2,871	Five or Fewer	24.49%	23.50%	26.64%	25.48%	N.A.

* Information presented prior to May 1, 2011 pertains to portfolios managed by the Portfolio Managers while affiliated with prior firms. The presentation conforms to GIPS® guidelines regarding the portability of investment results.

N.A. – Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

Mid-Cap Composite contains fully discretionary equity accounts that follow the mid-cap style. Mid-Cap Composite represents portfolios that seek long-term total return through capital appreciation by investing primarily in mid-cap stocks. For comparison purposes the composite is measured against the S&P MidCap and Russell MidCap indices. The S&P MidCap is a market value weighted total return index that represents the performance of the medium-capitalization sector of the U.S. Securities market. The Russell MidCap is a market value weighted total return index that represents the midcap segment which measures the performance of the 800 smallest companies in the Russell 1000 index. Both indices are representative of the types of equity assets invested by Fairpointe Capital. Market indices are unmanaged and do not reflect the deduction of fees. You cannot invest in an Index and the performance of the Index does not represent the performance of any specific investment. The minimum account size for this composite is $2.5 million. Prior to May 1, 2011 the account minimum was $5 million. Effective March 31, 2013, the account minimum has gone back to $5 million.

Fairpointe Capital LLC (Fairpointe) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Fairpointe has been independently verified for the periods May 1, 2011 through December 31, 2019.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Mid-Cap composite has been examined for the periods May 1, 2011 through December 31, 2019. The verification and performance examination reports are available upon request.

Fairpointe Capital is an independent registered investment adviser. The firm maintains a complete list of composite descriptions which are available upon request. Please send inquiries to mkatauskas@fairpointecapital.com or call 312-477-3300.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. Market, economic, company, and industry specific conditions are considered during the investment selection process. This was a period of generally rising security prices.

The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of management fees and include the reinvestment of all dividends, capital gains, and other earnings. Gross returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Net of fee performance is calculated using actual fees. The annual composite dispersion is an asset-weighted standard deviation calculated for the accounts in the composite the entire year. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The investment management fee schedule for the composite was 1.0% on the first $10 million and 0.65% on the remainder. Effective March 31, 2013, the fee schedule is 0.85% on the first $10 million and 0.65% on the remainder. Actual investment advisory fees incurred by clients may vary.

The three-year annualized ex-post standard deviation - December 31, 2019 - composite is 17.85% and 14.46% S&P MidCap and 12.89% Russell MidCap; December 31, 2018 - composite is 16.63% and 13.32% S&P MidCap and 11.98% Russell MidCap; December 31, 2017 - composite is 15.71% and 10.91% S&P MidCap and 10.36% Russell MidCap; December 31, 2016 - composite is 15.87% and 12.23% S&P MidCap and 11.55% Russell MidCap; December 31, 2015 - composite is 14.30% and 11.70% S&P MidCap and 10.85% Russell MidCap; December 31, 2014- composite is 13.4% and 11.1% S&P MidCap and 10.1% Russell MidCap; December 31, 2013 - composite is 18.4% and 15.0% S&P MidCap and 14.0% Russell MidCap; December 31, 2012 - composite is 20.6% and 17.9% S&P MidCap and 17.2% Russell MidCap; December 31, 2011 - composite is 25.0% and 21.9% S&P MidCap and 21.6% Russell MidCap, respectively.

The Mid-Cap Composite was created May 1, 2011. Performance presented prior to May 1, 2011 occurred while the Portfolio Managers were affiliated with prior firms and the Portfolio Managers were the only individuals responsible for selecting the securities to buy and sell.