



Small Cap Value Equity

Overview

U.S. equities performed poorly in the fourth quarter. What began as a modest pullback devolved into a market rout in December. In the end, it was the worst fourth quarter since 2008, with all major market indices posting ugly double-digit declines. Not surprisingly, investors flocked to perceived safe havens, helping large cap stocks outperform mid and small cap issues. Every economic sector in the Russell 2000® Value Index (RUJ) posted negative returns in the fourth quarter with the bond proxy sectors Consumer Staples and Utilities performing best and the RUJ's Energy constituents declining by more than 40%.

Portfolio Performance & Developments

Cooke & Bieler's Small Cap Value portfolio returned -18.36% gross of fees (-18.58% net of fees) versus the RUJ's -18.67% return for the fourth quarter. Weak portfolio positioning was offset by strong stock selection. Although the strategy did slightly outperform the RUJ, we are disappointed by such modest outperformance during such a meaningful market decline. That said, early downturns are often indiscriminate, with investors fleeing to seemingly demand defensive sectors and industries with less regard for underlying business quality or valuation. Though on the surface counterintuitive, our experience has been that the portfolio's quality characteristics provide little protection in these downdrafts. Typically, the defensiveness inherent in our investment approach reveals itself in more protracted and challenging economic and market environments.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)		Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Helen of Troy	3.9	0.2	6	Colfax	3.4	-42.0	-161
Entegris	2.1	-3.4	3	Schweitzer-Mauduit	3.2	-33.6	-118
Hexcel	0.2	0.8	2	Air Lease	2.5	-33.9	-92
RenaissanceRe	2.5	0.3	1	PGT Innovations	3.1	-26.6	-88
Penske Auto Group	0.0	-3.4	0	Syneos Health	3.6	-23.7	-82

Source: FactSet

Past performance is not indicative of future results. The performance attribution is an analysis of a representative Small Cap Value institutional portfolio's gross of fees return relative to the Russell 2000® Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's Small Cap Value clients. To obtain the calculation's methodology and a list showing every holding's contribution to the overall account's performance during the quarter, contact your client service representative or email your request to contact@cooke-bieler.com.

Largest Contributors

Helen of Troy (HELE), a diversified consumer goods company with leading positions in various niche categories, was the largest contributor for the quarter. HELE reported strong sales growth in the Housewares and Healthcare and Home Environment segments, offsetting weakness in the Personal Care and Beauty segment.

Entegris (ENTG), a provider of products and systems that purify, protect, and transport critical materials used in the semiconductor device fabrication process, was the second largest contributor. ENTG benefited from its more consumables-oriented sales mix as investors grew concerned about the semiconductor cycle. We continued building our position on stock price weakness.

Hexcel (HXL), a leading producer of light weight, high-performance structural materials for use in commercial aerospace, space and defense, and industrial applications, was the third largest contributor. We initiated our position late in the fourth quarter, so its position as a top contributor was more due to timing during a major market pullback than company-specific developments.

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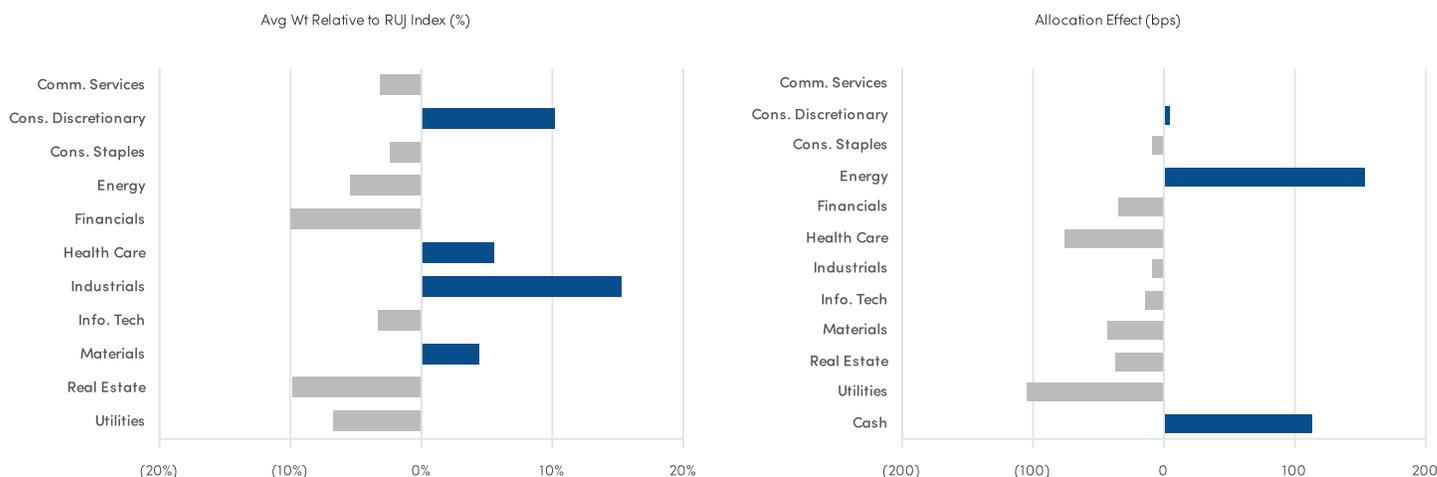
Largest Detractors

Colfax (CFX), an industrial company focused on large-scale air and gas handling equipment, welding, and other metal fabrication products and services, was the largest detractor for the quarter. CFX announced a significant acquisition in the quarter, one we believe makes long-term strategic sense and should add value over time, but which introduced complexity and financing needs at a moment the market was receptive to neither.

Schweitzer-Mauduit (SWM), a leading supplier to the tobacco products industry, was the second largest detractor. SWM faced margin pressure due to input cost inflation and the final stages of rationalization in one of their facilities. In our view, stock price weakness is less due to fundamental results and more to general weakness in small cap Materials and fears of continued input cost inflation.

Air Lease (AL), a leading aircraft lessor focusing on new, mostly narrow body aircraft, was the third largest detractor despite reporting an uneventful quarter and no change to their fundamental outlook. We believe the stock price weakness is due to investor fear of weakening global macroeconomic conditions affecting aircraft demand growth and airline credit quality rather than fundamental results in the business.

Sector Positioning



Source: FactSet
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The strategy's positioning was a modest headwind to relative results in the quarter, with a sizeable benefit from its underweight in Energy overshadowed by the negative impact of its overweight in Health Care and Materials and its underweight in Real Estate and Utilities. This headwind was more than offset by favorable stock selection effect, which was particularly strong in the Health Care and Consumer Discretionary sectors. With the exception of market capitalization – which clearly favored larger cap issues – there existed no discernable pattern across style factors.

Initiations

Glacier Bancorp (GBCI) is a regional bank holding company providing commercial banking services in communities across the Mountain West region. GBCI's focus on smaller markets and their retention of familiar brand names gives them an advantage over larger banks, resulting in high deposit market shares in their core markets and attractive funding costs.

Hexcel (HXL) develops, manufactures and markets lightweight, high-performance structural materials for use in commercial aerospace, space and defense, and industrial applications allowing their customers to make lighter, more durable and more efficient products. HXL benefits from increased composite content in aircraft and their competitive advantages include long-standing customer relationships, strict aerospace qualifications, and the significant and compounding nature of investments in R&D and capital expenditure. Additionally, the company maintains a conservative balance sheet, and long-term management incentives align decision-makers with shareholders.

Eliminations

Penske Automotive Group (PAG), **Tetra Tech (TTEK)**, and **United Natural Foods (UNFI)** were each sold to make room for more compelling ideas.



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Outlook

While the strategy outperformed the RUJ by a healthy margin for the full year and has outperformed by a greater annualized margin over the past five years, we believe it still has quite a bit of potential energy as we enter 2019. A byproduct of recent activity and the market pullback is a portfolio offering exceptional value and considerable appreciation potential. In addition, among the major style indices, valuations for small cap value stocks have contracted the most over the past year. With the portfolio trading at a discount to its benchmark, we remain confident in the portfolio's relative prospects heading into 2019.

Sources: Bloomberg; FactSet; FTSE Russell; Jefferies

Past performance is not indicative of future results. The material presented represents the manager's assessment of the Small Cap Value institutional portfolio and market environment at a specific point in time and should not be relied upon by the reader as research or investment advice regarding any particular security or sector. The above commentary and portfolio attribution are based on a representative Small Cap Value institutional portfolio for the quarter ending 12/31/18. The portfolio attribution is gross of fees. Certain client portfolios may or may not hold the securities identified above due to the respective account's guidelines, restrictions, required cash flows, or other relevant considerations. The performance attribution is an analysis of the portfolio's return relative to the Russell 2000® Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's Small Cap Value clients. To obtain the calculation's methodology and a list showing very holding's contribution to the overall account's performance during the quarter, contact your client service representative or email your request to contact@cooke-bieler.com.

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