



# Small Cap Value Equity

## Overview

U.S. equities performed extremely well in the first quarter, with small cap stocks off to their best start since 1991 and posting their best overall quarter since Q4 2011. Emboldened by the Fed's accommodative pivot, investors shrugged off concerns about the economy, creating an environment that was the polar opposite of last year's fourth quarter. The Russell 2000® Value Index (RUJ) returned 11.93%, with every sector posting strong gains – though the sectors and stocks that performed worst during the late 2018 sell-off tended to benefit most from this quarter's profound change in sentiment. Unlike in Q4, growth outperformed value.

## Portfolio Performance & Developments

Cooke & Bieler's Small Cap Value Strategy returned 15.02% gross of fees (14.75% net of fees), handily beating the RUJ's 11.93% return for the first quarter and adding to the healthy lead it accumulated in 2018. Favorable stock selection – positive in six of eight sectors in which the portfolio had weight – explained more than all of the positive relative result this quarter, with particular strength in Industrials, Materials and Healthcare. Valuations normalized for holdings that were unduly punished late last year, with the two largest contributors this quarter having been the portfolio's biggest detractors in Q4 2018. More broadly, solid fundamental progress across most of the portfolio's holdings also contributed to the strategy's excess return.

## Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Schweitzer-Mauduit	3.6	56.3	156
Colfax	3.7	42.0	132
Winnebago	4.1	29.2	109
Varex Imaging	2.8	43.1	105
Syneos Health	2.8	31.5	100

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Nautilus	0.5	-35.6	-81
Mednax	2.2	-17.7	-43
PGT Innovations	3.0	-12.6	-32
Helen of Troy	2.9	-11.6	-31
National Western Life	1.5	-12.7	-17

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](mailto:contact@cooke-bieler.com).

## Largest Contributors

**Schweitzer-Mauduit (SWM)**, a Materials holding that supplies the tobacco products industry as well as the automotive, infrastructure and filtration industries, was the largest contributor in the quarter. It was a leading portfolio detractor in Q4 2018 as investors grew concerned about the health of its industrial end markets and higher commodity input costs. However, fourth quarter organic growth and margin performance were strong, and guidance implies that this strength should continue.

**Colfax (CFX)**, a designer and manufacturer of air/gas handling and fabrication products, was the second largest contributor. After significantly detracting from returns in Q4 2018, short-term market concerns tied to an acquisition lifted as the company started to execute on financing plans. Further transparency on pro-forma expectations also helped shift investor sentiment.

**Winnebago (WGO)**, a top U.S. manufacturer of recreational vehicles, was the third largest contributor. Investor concern about a slowdown in the RV industry caused the stock to be one of the leading portfolio detractors in 2018. The stock has recovered strongly given evidence of healthier dealer inventory positions in 2019 as well as continued share gains for Winnebago but remains one of the most attractive holdings in the portfolio.

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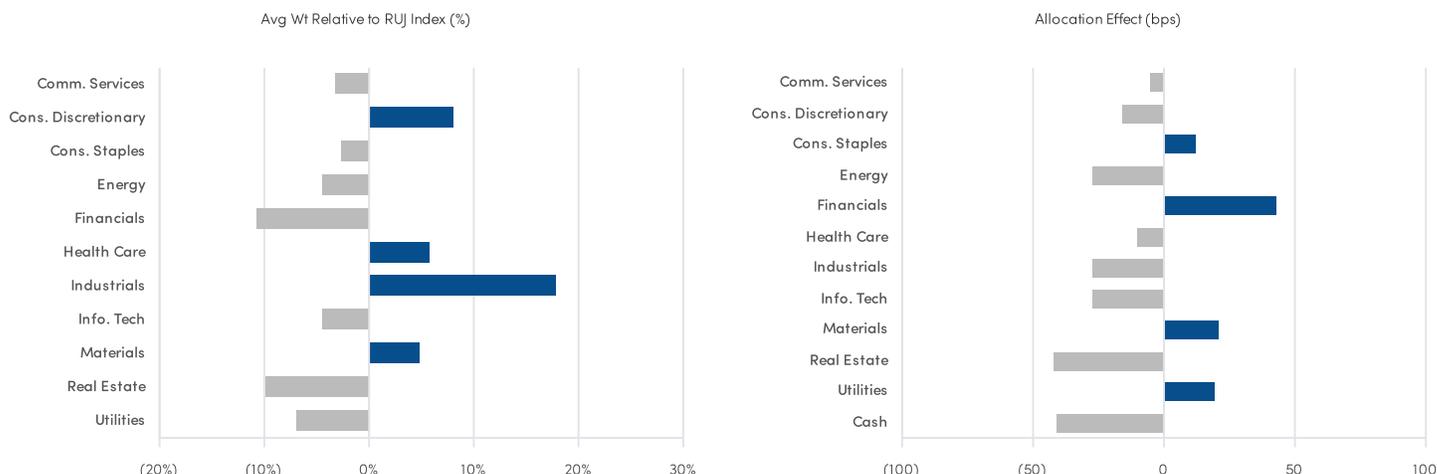
## Largest Detractors

**Nautilus (NLS)**, a leading designer and manufacturer of home fitness equipment, was the largest detractor in the quarter. The company posted disappointing fourth quarter results that invalidated our thesis. New product introductions have failed to resonate with consumers in its direct-to-consumer segment and, with little confidence in management’s ability to restore growth, we decided to eliminate the position.

**Mednax (MD)**, a leading national physician group practice provider of neonatal, anesthesia, and radiology services, was the second largest detractor. MD has been wrestling with several macro headwinds that have pressured profitability. When these headwinds abate we expect the stock will more appropriately reflect the free cash flow generative power of the business and management’s actions to grow revenue organically by expanding relationships with hospitals and improve profitability by cutting general and administrative costs and restructuring physician compensation programs.

**PGT Innovations (PGTI)**, the leading manufacturer of impact-resistant windows – serving primarily the Florida residential market – was the third largest detractor. Though reported results were very strong, a portion of that fundamental strength owed to the favorable impact of hurricane activity in the Florida market, making comparisons difficult versus 2018. Long-term demographic trends and adoption rates for PGTI’s products remain favorable and we made the stock a top position in the quarter.

## Sector Positioning



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 sector return relative to the Russell 2000® Value Index. Please see additional performance disclosures at the end of this document.

Sector allocations, a byproduct of Cooke & Bieler’s bottom-up process, offset approximately a quarter of the positive stock selection result in Q1. While underweight positions in Financials and Consumer Staples – the RUJ’s worst performing sectors – and an overweight in Materials were additive, results were mostly negative elsewhere. The strategy’s underweight in the bond proxy sectors generated mixed results, with a positive allocation effect in Utilities, but negative effect in Real Estate. The portfolio’s modest level of frictional cash was also an outsized negative given the quarter’s strong positive showing.

## Initiations

**American Woodmark (AMWD)** is the second-largest residential cabinet and vanity manufacturer in the U.S. as well as a former Cooke & Bieler small cap portfolio holding. AMWD is a demonstrated share gainer thanks to its competitively-advantaged, low-cost supply chain. Having recently acquired a leading manufacturer of opening price point, in-stock cabinetry – a category in which the AMWD has not previously participated – management intends to leverage its unique installation network and existing relationships in the new construction channel to penetrate the entry-level housing and multifamily market segments.

**Essent Group (ESNT)** is a private mortgage insurer with a focus on managing credit risk through disciplined and granular underwriting on the front-end and the use of reinsurance on the back-end. As a relatively new entrant, ESNT benefits from an improved industry structure, including a new regulatory regime, new capital market solutions, and more rational competitors all of which has led to improved industry economics resulting in a solid compounder with good downside protection through the credit cycle. We were excited to initiate at ~1.5x current book value.



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## Eliminations

**Nautilus (NLS)** tracked poorly against our initial investment thesis and we eliminated the position.

## Outlook

In the context of increasingly conflicting economic signals and a big jump in valuations resulting from the strong first quarter rally, our market outlook for the remainder of this year is somewhat guarded. Amidst growing uncertainty, we see a mixed environment, likely including increasing volatility. This backdrop should provide active investors with opportunities to add value through disciplined stock selection. We believe the portfolio continues to be positioned to outperform given its attractive combination of quality characteristics and reasonable valuation.

Sources: Bloomberg; FactSet; FTSE Russell; Jefferies; The New York Times

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 3/31/19. 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](mailto:contact@cooke-bieler.com).

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