Cooke & Bieler

Q1 2021

Small Cap Value Equity

Overview

U.S. equity markets continued to surge during the first quarter of 2021. Intensifying economic momentum, another enormous dose of fiscal stimulus, highly accommodative monetary policy, and expanding vaccine availability further fueled the market's appetite for risk. That appetite was voracious for the stocks of companies poised to benefit most from economic reopening and recovery, keeping small cap well ahead of the pack along with cyclical and financial issues. The resurgence of value stocks that began late last year also intensified, with value beating growth by the widest margin since Q1 2001. Within value indices, low valuation and low quality led the charge – they were pronounced drivers at the lower end of the capitalization spectrum where nearly a fifth of all companies are non-earning.

Portfolio Performance & Developments

Cooke & Bieler's Small Cap Value Strategy returned 16.30% gross of fees (16.02% net of fees), underperforming the Russell 2000® Value Index, which returned 21.17%. Broadly negative stock selection effect overwhelmed the positive impact of sector allocation effect and drove more than all of the portfolio's shortfall. Only five holdings posted negative performance in the quarter, however, the portfolio was unable to keep up with the benchmark and the surging prices of low quality stocks. Consumer Discretionary stocks – one of the largest sector weights in the portfolio – posed the greatest headwind, with Helen of Troy and Stoneridge lagging most. Industrials and Financials holdings such as IAA, Woodward, and FirstCash also detracted from relative results. Information Technology holdings, particularly Onto Innovation, were the relative bright spot. Over the trailing twelve months since the pandemic crash, the strategy has modestly lagged the benchmark. While the portfolio has generated very strong absolute performance over that period, the positive impact of sector allocation effect has not quite offset the drag from negative stock selection effect. Over longer periods, the portfolio's performance remains well ahead of the benchmark.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
American Eagle	3.1	46.4	144
Winnebago	3.9	28.2	108
Glacier Bancorp	3.2	24.4	83
Onto Innovation	2.0	38.2	76
PGT Innovations	3.1	24.1	73

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
IAA	2.5	-15.1	-32
FirstCash	2.9	-5.8	-11
Helen of Troy	2.8	-5.2	-7
Woodward	2.2	-0.6	-3
WSFS Financial	0.1	-0.5	1

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

American Eagle Outfitters (AEO), a leading teen and young adult retailer operating through the American Eagle and Aerie brands, was the largest contributor. AEO reported strong earnings despite ongoing COVID-related store closures and outlined a plan to double sales in their Aerie brand over the next three years while improving profitability.

Winnebago (WGO), a leading manufacturer of recreational vehicles, was the second-largest contributor. WGO continued to benefit from strong overall demand for recreational vehicles and to gain share in its towables segment. Motorized segment margins have also improved dramatically after several years of supply chain initiatives.

Glacier Bancorp (GBCI), a regional bank operating as a collection of community banks in the Mountain West, was the third-largest contributor. GBCI reported solid results for the quarter and the year, having navigated the pandemic with minimal impact. The Mountain West region is poised to rebound strongly and should continue to benefit from strong in-migration trends.

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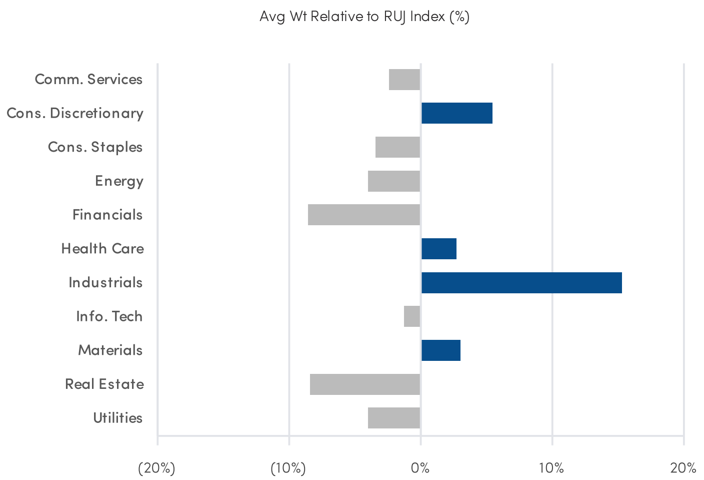
Largest Detractors

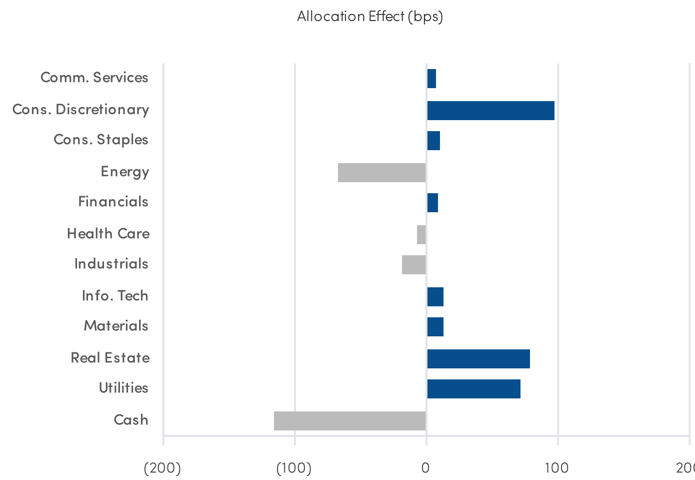
IAA (IAA), an owner and operator of a leading auction marketplace for the sale of total loss, damaged, and low value vehicles, was the largest detractor. IAA underperformed as investors drove the stock's valuation down, potentially due to concern over the sustainability of recent elevated average selling prices, worry about short-term disruption related to winter storms in Texas, or disappointment that management did not provide guidance due to COVID-19 related uncertainty.

FirstCash (FCFS), the largest pawn shop operator in North America and Mexico, was the second-largest detractor. FCFS reported solid fourth quarter results but noted that demand for pawn loans would likely be restrained by a fresh round of stimulus payments. Over time, we expect pawn loan demand to recover to pre-pandemic levels and FCFS management to deploy the business' considerable cash flow in value-added ways.

Helen of Troy (HELE), a diversified consumer and household products company, was the third-largest detractor. HELE was a net beneficiary of pandemic-driven demand, but its shares have lagged more recently as investors worried about difficult comparisons. However, the company's organic growth rate and margin profile should continue to benefit on a long-term basis thanks to meaningful investment in product innovation and shared services across segments. With a very conservative balance sheet, HELE is also in a good position to engage in opportunistic M&A activity and share repurchases.

Sector Positioning





Source: FactSet
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Sector allocation effect was additive for the quarter, with the majority of sectors contributing on a relative basis. Leading the pack was Consumer Discretionary, one of the best performing sectors and one of the portfolio's largest overweights. Perceived safe-haven sectors did not fare as well during the continued market exuberance, so the strategy's underweight to Real Estate and Utilities was also additive. Partially offsetting these positive results, the portfolio's underweight in Energy was again a headwind given the sector's very strong performance during the quarter. The overweight to Industrials and Health Care, two of the weaker performing sectors, also detracted from relative results.

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Initiations

Armstrong World Industries (AWI) is the leading North American manufacturer of non-residential ceiling systems. Its pricing power, mix trends, and margins are among the most favorable and consistent in the building products industry. AWI's commercial new construction and renovation end markets are depressed due to COVID-related weakness, but the favorable competitive dynamics and profitability of AWI's mineral fiber ceilings business should persist after non-residential construction activity recovers. Mix tailwinds should accelerate as a broader set of customers seek out more differentiated ceiling tiles and systems designed to improve air quality.

WSFS Financial (WSFS) is the largest locally-headquartered bank in the Philadelphia metropolitan area. Through its recent acquisitions of Beneficial Bank and Bryn Mawr Trust, the company has gained significant in-market scale which should lead to improved margins over time. In addition, WSFS has attractive sources of non-interest income, such as their leading trust and wealth management platform and their Cash Connect business, which manages cash holdings for thousands of ATMs.

Eliminations

Cohu (COHU) and **NV5 Global (NVEE)** reached their price targets and were eliminated.

TCF Financial (TCF) was eliminated to make room for better opportunities in the wake of their acquisition by Huntington Bancshares.

Outlook

Markets are clearly forecasting a strong recovery fueled by pent up consumer demand and ongoing fiscal and monetary stimulus. However, with indices well above pre-pandemic levels, even a strong recovery may not be enough to sustain further gains. Though investors are prone to forget it in moments of enthusiasm, valuations matter – and large parts of the market are currently expensive even relative to optimistic assumptions. The most extreme examples of this disconnect are currently found among smaller capitalization stocks, where in some cases social media has driven waves of buying, willfully oblivious to any fundamental assessment of value. However, valuations are stretched among larger capitalization stocks as well, and at current prices we are quite sure many of these investments will turn out badly.

While markets are efficient over the long run, in the short term they are driven by human emotion and it is impossible to predict when fickle natured sentiment will turn. The wise investor must remain focused on business fundamentals and valuations. A year ago – in light of a once-a-century pandemic – we were working diligently to re-underwrite the portfolio, with a focus on companies' abilities to survive a severe and prolonged downturn. Today, our challenge is finding value in a market that has quickly forgotten about risk. Regardless of the market environment, the core features of our process and discipline remain consistent: exhaustive research to identify businesses that can compound value, insistence on conservative balance sheets that can withstand economic shocks, and a patient focus on buying businesses below intrinsic value.

Sources: Advent Portfolio Exchange, Bank of America Global Research, Bloomberg, FactSet, Jefferies, Russell, The Wall Street Journal, Zacks Investment Research

Additional Cooke & Bieler Small Cap Value Performance Disclosures