



Small Cap Value Equity

Overview

Stocks turned in their worst performance since the onset of the pandemic two years ago as investors processed a seeming tsunami of bad news and pushed all major indices into negative territory. The Russian invasion of Ukraine signaled not just the largest European war in 75 years, but perhaps the most aggressive sanctions regime in history. The combination touched off a price surge in oil and other commodities, further fueling inflationary trends that were already running at 40-year highs and sending 10-year treasury yields to their highest level in two years. Recent history would suggest the Federal Reserve would react to these shocks by communicating their ability and willingness to ease monetary conditions to protect the economy. However, with their COVID-era stimulus measures still very much in force and inflation at worrying levels, the Fed instead embarked on what is forecast to be an extended tightening process by raising rates a quarter of a point in March.

The tumultuous macro backdrop led to considerable volatility and a wide dispersion of returns across sectors. The markets sold off sharply in January and February. Growth indices were particularly hard hit, as investors began to price in the impact of higher rates on these long-duration assets. March, however, brought a wave of buying, spurring a partial recovery in growth and pushing value indices almost to break-even for the quarter. As is to be expected in turbulent times, larger capitalization stocks generally performed better than smaller ones. Among sectors, Energy was the standout with soaring oil prices driving shares across the capitalization spectrum up more than 35%. Conversely, investors worried about the impact of inflation, rising rates, and general uncertainty on consumer spending and corporate margins, which drove shares of Consumer Discretionary companies down close to 10% for the quarter.

Portfolio Performance & Developments

Amidst another tumultuous quarter, Cooke & Bieler's Small Cap Value Strategy underperformed the Russell 2000® Value Index, posting -10.06% gross of fees (-10.30% net of fees) against a -2.40% return for the benchmark. The portfolio's struggles were attributable to meaningfully negative stock selection and sector allocation effects. Industrials and Energy holdings detracted the most, owing mostly to an overweight position in the particularly hard hit building products industry within Industrials and greater economic exposure to drilling activity as opposed to commodity prices within Energy. Consumer Discretionary holdings such as Winnebago, American Eagle, and Helen of Troy also weighed on results as new recessionary fears only exacerbated existing supply chain and inflation concerns. Information Technology holdings posed a headwind to the portfolio as well, while stock selection within Financials was a modest bright spot.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)		Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Reliance Steel	1.7	14.7	35	Winnebago	4.1	-27.7	-126
Woodward	2.7	14.3	35	American Eagle	2.7	-33.0	-97
BWX Technologies	2.1	13.0	28	Helen of Troy	4.1	-19.9	-85
Selective Insurance	1.8	9.5	18	American Woodmark	2.8	-24.9	-76
Stoneridge	1.7	5.2	14	IAA	2.9	-24.4	-74

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.





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Largest Contributors

Reliance Steel (RS), the largest metal service center distributor in North America, was the largest contributor. Solid execution with a highly favorable inflationary backdrop led to record sales, margins, and EPS during 2021. We eliminated the position during the quarter as the price approached our estimate of fair value.

Woodward (WWD), a supplier of energy and motion control systems to the aerospace and industrial industries, was the second-largest contributor. While results continue to be negatively affected by supply chain disruptions and labor shortages, WWD is poised to benefit from the ongoing commercial aerospace recovery due to its strong content on narrowbody aircraft and positioning in the aftermarket. In the quarter, WWD announced a significant share repurchase authorization and highlighted its strong free cash flow generation potential over the next five years at a well-received investor day.

BWX Technologies (BWXT), a provider of nuclear reactors for submarines and aircraft carrier propulsion, was the third-largest contributor. BWXT rebounded as its quarterly results and 2022 guidance pointed toward free cash flow improvement after years of elevated investment. The company also benefited from a shift in investor views on defense spending due to the Russia-Ukraine conflict.

Largest Detractors

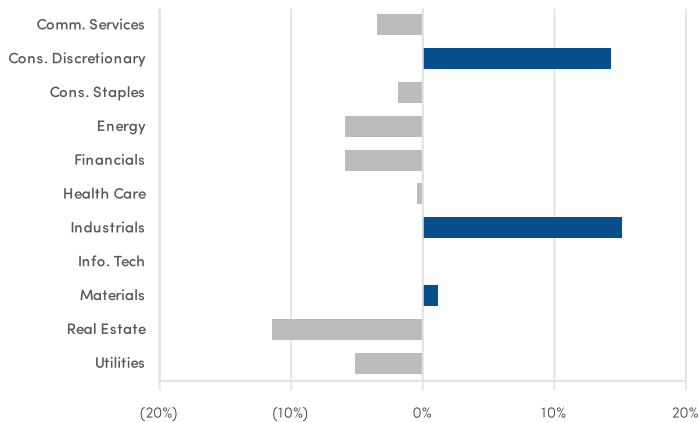
Winnebago (WGO), a leading manufacturer of recreational vehicles, was the largest detractor. WGO continues to post strong and improving fundamental results, but investor fears of significantly weakening demand weighed on the stock price. This fear is not unfounded, but overlooks the company's growing market share and organic white space opportunities, the structural margin progress in its motorhome division, its recent marine segment acquisition, and the positive secular growth prospects of the RV industry.

American Eagle Outfitters (AEO), a leading teen and young adult retailer operating through the American Eagle and Aerie brands, was the second-largest detractor. AEO reported strong sales and margins, but results were dampened by increased product and shipping costs. Investors are concerned AEO will struggle to pass on cost increases and will be forced to sacrifice either margins or market share as well as the potential for a consumer recession.

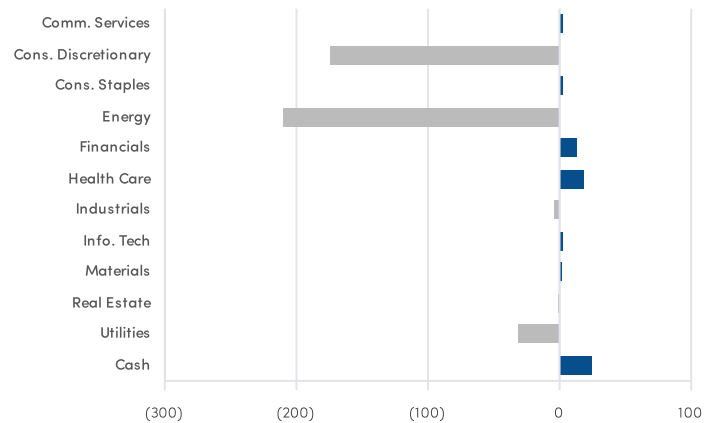
Helen of Troy (HELE), a diversified consumer and household products company, was the third-largest detractor. As the pandemic fades, HELE has seen above average demand for its home healthcare products normalize. Investors, however, are overlooking the offsetting benefit of economic reopening on its highest margin products, the resilience of its housewares segment, the accretion from its latest acquisition, and the market share momentum in its beauty franchise.

Sector Positioning

Avg Wt Relative to RUJ Index (%)



Allocation Effect (bps)



Source: FactSet
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Sector allocation effect detracted from relative performance in the first quarter. The portfolio's meaningful underweight to the Energy sector, by far the standout performer within the benchmark with a return of over 40%, and considerable overweight to Consumer Discretionary, the worst performing sector within the benchmark with a return of -14%, explained more than all of the negative sector allocation effect. The portfolio's underweight to the Health Care and Financials sectors generated a modest positive offset.

Initiations

Gentex (GNTX) is a dominant provider of interior and exterior automatic-dimming mirrors for the automotive industry, with a 90% market share. The company also sells garage opener modules, dimmable aircraft windows, and commercial smoke detectors for the fire protection industry. GNTX's core competencies in chemistry and coatings, glass processing, electronics, vision systems, software design, and automated assembly create optionality in its core market as well as in new markets. We believe that its strong competitive position, good secular growth prospects, strong balance sheet, and disciplined program for returning capital to shareholders make it an attractive holding.

Eliminations

Reliance Steel (RS) reached its price target and was eliminated.

Outlook

No investment style outperforms against every market backdrop. However, every period of sustained underperformance requires honest introspection about the team's analysis and process as well as an open minded search for potential improvements. With underperformance concentrated in the portfolio's Consumer Discretionary and Industrials holdings, we have re-underwritten these positions, evaluating the drivers of demand for their products, their competitive positions, and pricing power in an inflationary environment. While the market seems to be pricing in a severe consumer recession lasting indefinitely, along with severe margin pressure driven by supply chain disruption and inflation, we believe the portfolio holdings' company-specific long term fundamental drivers remain firmly intact. Moreover, even if the earnings of our holdings were to decline by more than half, certain of these businesses would still trade at single digit multiples of EPS. This combination of attractive fundamentals and enticing valuations justifies the portfolio's concentration in these sectors and sets a strong foundation for longer term prospective investment returns. Conversely, the market's assessment of the Energy sector – the other big driver of portfolio underperformance – has overshot sustainable reality, and here we remain confident in our relatively subdued long term view of these businesses and the resulting underweight position.

While recent performance has been very disappointing, the fundamental performance of our portfolio holdings remains strong, and in most cases has continued improving. Which is not to say that its pro-cyclical tilt is impervious to broader economic weakness, but our experience is that it is better to own businesses that can outperform across cycles rather than guess at short term economic developments. This differentiated perspective and positioning has worked against the portfolio's performance recently, but these unique views have also been the source of significant longer term historical outperformance. Our experience is that patience and steadfast focus is generally rewarded over time.

Sources: APX, Bloomberg, CNBC, The Economist, FactSet, The New York Times, The Wall Street Journal

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 3/31/22. 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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