



Small Cap Value Equity

Overview

U.S. equity markets continued higher in the third quarter on the heels of further government stimulus, improving economic data, encouraging readouts from COVID-19 vaccine trials, and better clinical outcomes for COVID-19 patients. Though the trend reversed in September, growth stocks again led the charge, with the Russell 2000® Growth Index up 7.16% for the three-month period versus 2.56% for the Russell 2000® Value Index. Within the value universe mid cap stocks once again fared best, narrowing the lead amassed by their large cap peers during the Q1 market decline. Given continued resilience in consumer spending and increasing evidence of economic recovery, the generally broad-based market advance included particular strength among Consumer Discretionary and other economically sensitive constituents, though Energy stocks declined meaningfully in the face of persistently low oil prices.

Portfolio Performance & Developments

After a strong start to 2020, Cooke & Bieler's Small Cap Value Strategy returned 0.87% gross of fees (0.62% net of fees), underperforming the Russell 2000® Value Index. Allocation effect was strongly positive, but significantly negative stock selection effect was an offset. The portfolio's Consumer Discretionary and Health Care holdings detracted most, with a number Q2 standouts including Winnebago and Hill-Rom surrendering some of their second quarter strength. Financials, Materials, and Industrials also detracted from relative results. Energy was a bright spot for stock selection thanks to the strong performance of the portfolio's newest holding against an otherwise dismal sector backdrop. Despite lagging in Q3, the portfolio is still solidly ahead of the benchmark YTD.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)		Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
American Eagle	3.1	35.9	97	Winnebago	3.8	-22.3	-92
Gildan Activewear	3.5	27.0	76	Hill-Rom	2.6	-23.7	-67
IAA	2.6	35.0	75	TCF Financial	3.0	-19.6	-64
PGT Innovations	3.9	11.7	52	FirstCash	2.8	-14.8	-49
Colfax	3.4	12.4	44	Hexcel	1.0	-25.8	-30

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. Although disruptions caused by widespread store closures negatively affected reported results, AEO posted solid underlying fundamentals. Their Aerie brand in particular demonstrated strong momentum.

Gildan Activewear (GIL), the largest basic apparel manufacturer, was the second-largest contributor. GIL recovered strongly after its poor performance in the second quarter. End markets for its blank printwear garments showed signs of life and management reiterated its pre-COVID margin targets.

IAA (IAA), an owner and operator of a leading auction marketplace for the sale of total loss, damaged, and low value vehicles, was the third-largest contributor. Sales in the second quarter were more resilient than feared, as higher revenue per vehicle meaningfully offset lower volumes caused by COVID-19-related declines in driving activity. Industry volumes improved substantially further into the third quarter. IAA's profitability and cash generation capabilities remained promising despite the quarter's overall soft volumes.





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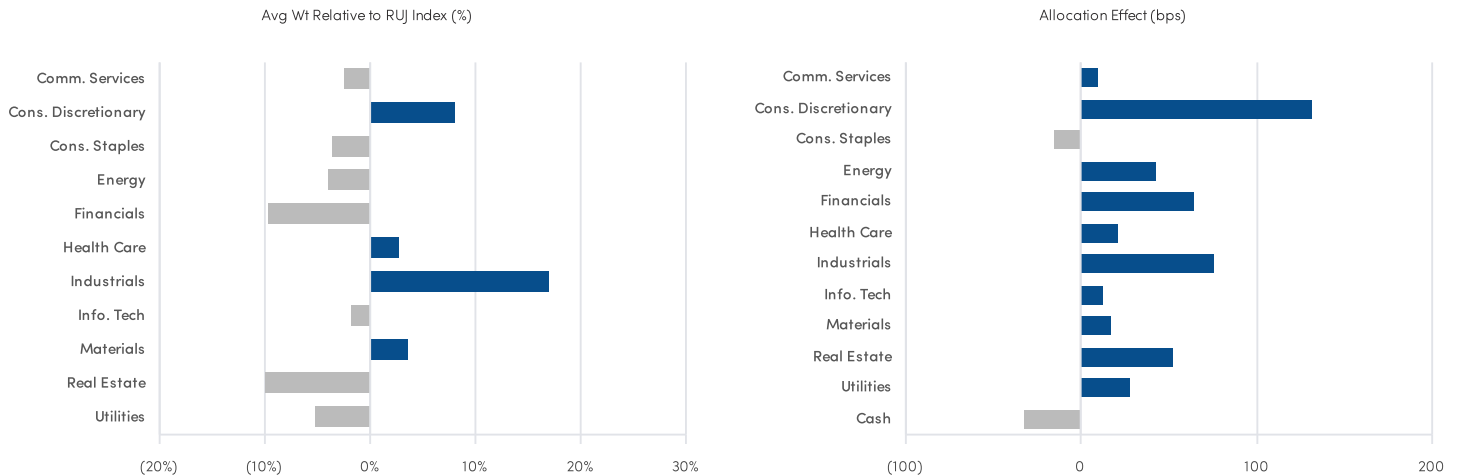
Largest Detractors

Winnebago (WGO), a leading manufacturer of recreational vehicles, was the largest detractor. WGO relinquished some of its strong second quarter price performance as investors questioned the sustainability of recent RV market strength. While near-term demand is clearly benefitting from COVID-related tailwinds, industry volumes remain well below previous peaks and Winnebago continues to win market share from larger peers.

Hill-Rom (HRC), a provider of hospital beds and patient monitoring devices, was the second-largest detractor. HRC's valuation contracted significantly from its second quarter levels due to uncertainty about the near-term demand for hospital beds.

TCF Financial (TCF), a Midwest bank with a strong deposit base and a diversified lending platform, was the third-largest detractor. TCF lagged during the quarter as a combination of falling interest rates and rising credit costs weighed on expectations for profitability. However, TCF's recent merger with Chemical Financial should provide them with cost saving opportunities that could offset falling rates and credit losses in their diversified and conservatively underwritten loan portfolio.

Sector Positioning



Source: FactSet
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Strong sector allocation effect benefitted the portfolio's relative results during the quarter. An overweight to Consumer Discretionary – by far the benchmark's best performing sector – contributed meaningfully as economies reopened and consumer confidence improved. An overweight to Industrials and underweight to Financials, Real Estate, and Energy were also additive. The Energy sector, which remains the weakest sector YTD, posted the Index's worst return by a large margin in the quarter and has been incredibly volatile this year – having been the worst performing sector in Q1, one of the best in Q2, and again the worst in Q3. The only sector that did not contribute to the portfolio's favorable allocation effect was Consumer Staples.





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Initiations

DMC Global (BOOM) is an explosives specialist with two segments: DynaEnergetics and NobelClad. DynaEnergetics manufactures industry-leading preassembled perforating guns used in the fracking of horizontal shale wells, while NobelClad is the top global producer of explosion-welded clad metal plates, which are used primarily in the petrochemical and oil and gas industries. The oil and gas industry presents a particularly attractive opportunity as the impetus to increase production efficiency demands higher perforation intensity. BOOM's balance sheet should enable the company to sustain R&D investment during this down cycle. Concerns about competition from other perforating gun manufacturers gave us the opportunity.

Onto Innovation (ONTO) provides optical process controls and yield enhancement tools to silicon wafer manufacturers, front-end chip manufacturers, and back-end chip packaging and testing companies. ONTO's products perform various functions, such as two- and three-dimensional macro defect inspection, optical critical dimension measurements, and process control analytics. The increasing complexity of leading-edge devices with ever-higher levels of silicon content has created demand for more sophisticated process control solutions across the entire semiconductor value chain. We believe that ONTO, as the leading provider of process control-enabling tools, will not only benefit from these secular industry trends but also drive market share gains and margin improvement as it grows into a larger entity.

Selective Insurance Group (SIGI) is a super-regional property and casualty insurance underwriter focused predominantly on small and mid-sized standard commercial lines. Utilizing a unique decentralized field model, SIGI has carved out a growing, profitable niche within a competitive landscape. Their disciplined pricing and conservative investment portfolio underpin a fundamentally stable business.

Eliminations

There were no eliminations this quarter.

Outlook

We remain generally constructive on the investing environment. The U.S. economy is exiting a recession and we expect the nascent recovery to persist as people slowly return to many pre-COVID routines, driven by human nature and emboldened by improving therapies and eventually vaccines. This process likely will not be linear, and we expect market volatility along the way, but highly accommodative fiscal and monetary policy should provide continuing support. Offsetting the improving fundamental backdrop to some degree are very high expectations embedded in valuations in parts of the market. As the economy normalizes, we expect investors will better appreciate the enormous valuation disparity between the stocks of companies that have benefitted from the pandemic and those that have been negatively impacted. We have selectively favored the latter group, emphasizing reasonably valued stocks of the best positioned, financially strong companies that possess both staying power and latent fundamental improvement potential. We expect the portfolio to perform well as underlying fundamentals progress and these characteristics are better recognized.

Sources: American College of Cardiology, APX, Axios, Bloomberg, FactSet, Forbes, NIH

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 9/30/20. 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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