



SMID 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 SMID Cap Value Strategy underperformed the Russell 2500™ Value Index, posting -8.08% gross of fees (-8.29% net of fees) against a -1.50% return for the benchmark. The portfolio's struggles were attributable to meaningfully negative stock selection and sector allocation effects. Consumer Discretionary holdings such as Winnebago, Helen of Troy, and American Eagle detracted the most as new recessionary fears only exacerbated existing supply chain and inflation concerns. Materials and Industrials holdings also weighed on results, owing mostly to underperformance by AerCap, IAA, and H.B. Fuller. Health Care holdings posed a headwind to the portfolio as well, while stock selection within Financials and Utilities 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) |
|----------------|----------------|------------------|--------------------------|----------------|----------------|------------------|--------------------------|
| Alleghany | 2.5 | 26.9 | 69 | Winnebago | 3.2 | -27.7 | -100 |
| Leidos | 2.4 | 21.9 | 49 | Helen of Troy | 3.6 | -19.9 | -77 |
| Woodward | 2.3 | 14.3 | 31 | AerCap | 3.0 | -23.1 | -74 |
| Atmos Energy | 2.1 | 14.8 | 28 | IAA | 2.1 | -24.4 | -59 |
| Reliance Steel | 1.3 | 14.7 | 27 | American Eagle | 1.7 | -33.0 | -58 |

Source: FactSet

Past performance is not indicative of future results. The performance attribution is an analysis of a representative SMID Cap Value institutional portfolio's gross of fees return relative to the Russell 2500™ Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's SMID 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.





SMID Cap Value Equity

Largest Contributors

Alleghany (Y), a reinsurance and specialty insurer, was the largest contributor. The company announced it was being acquired by Berkshire Hathaway at a 25% premium to both its book value and its pre-announcement stock price.

Leidos (LDOS), a leading provider of information technology and other services to the government, was the second-largest contributor. LDOS recovered from prior underperformance as investors shifted their views on defense spending in light of the Russia-Ukraine conflict, in addition to higher civilian budgets.

Woodward (WWD), a supplier of energy and motion control systems to the aerospace and industrial industries, was the third-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.

Largest Detractors

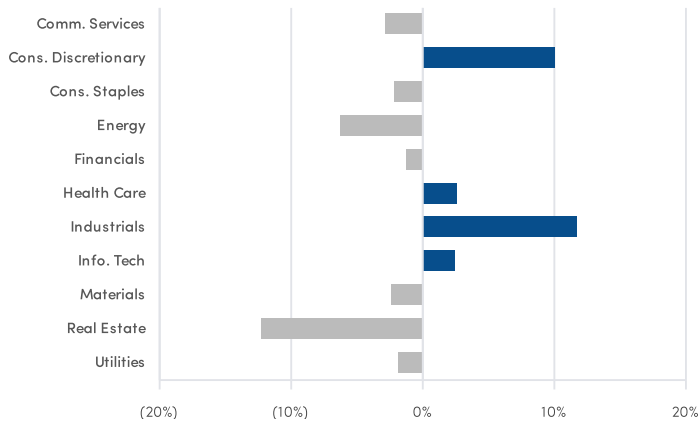
Winnebago (WGO), a leading manufacturer of recreational vehicles, was the largest detractor. WGO continues to post strong and improving fundamental results, but investor fears of significantly weakening demand weighed on the stock price. This fear is not unfounded, but overlooks the company's growing 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.

Helen of Troy (HELE), a diversified consumer and household products company, was the second-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.

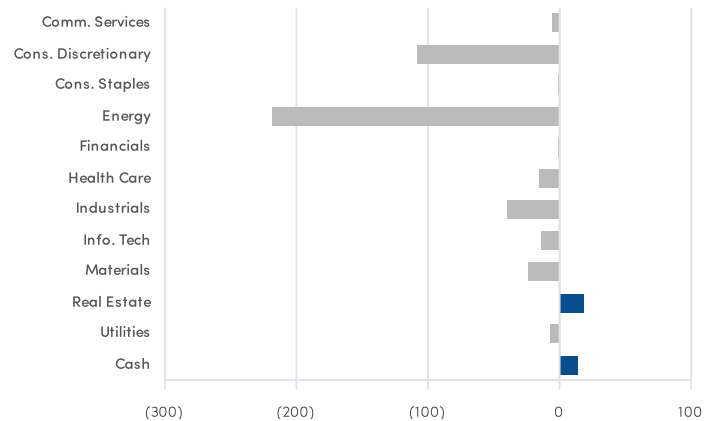
AerCap (AER), the largest independent aircraft lessor, was the third-largest detractor. Investors reacted negatively to the company's exposure to Russian airlines. In response to sanctions, Russian airlines have breached their contracts for aircraft and engines belonging to AER worth about \$2.5B. While the fate of these planes and resulting insurance claims is hard to assess, the company's overall exposure should prove to be manageable, and we believe AER remains well positioned longer term.

Sector Positioning

Avg Wt Relative to R25IV Index (%)



Allocation Effect (bps)



Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative SMID Cap Value institutional portfolio's gross of fees sector return relative to the Russell 2500™ Value Index. Please see additional performance disclosures at the end of this document.





SMID Cap Value Equity

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 -12%, explained nearly all of the negative sector allocation effect. The remaining headwinds to performance owed mostly to the overweight to pro-cyclical Industrials and the underweight to Materials. The portfolio's underweight to Real Estate generated a slight positive offset.

Initiations

Carmax (KMX) is an independent used car retailer that operates through both brick & mortar and online channels with over \$20 billion in annual sales. KMX sells vehicles through direct retail and wholesale auction channels, supporting its retail business with ancillary products such as financing, warranty, and service plans. The company's scale enables it to make more data-driven decisions on its inventory to avoid significant depreciation. We expect KMX to gain share in the fragmented used car market due to its low-friction customer experience, increasing use of technology, and willingness to leverage different business segments to achieve strong results for the company as a whole.

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 SMID 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 SMID 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 2500™ Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's SMID 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.

[Additional Cooke & Bieler SMID Cap Value Performance Disclosures](#)