



SMID Cap Value Equity

Overview

The second quarter was a bumpy ride for the U.S. stock market. The rally that began late last year continued through April, was upended in May by renewed concerns about the economy and a more protracted trade war, then was revived in June by the Fed's clear pivot toward monetary easing. The June rally was enough to push major indices into positive territory for the quarter, capping a strong first half of the year which saw stocks up double digits. Returns were strongest for large cap stocks, but otherwise underlying market dynamics lacked discernable themes. Against this backdrop the Russell 2500™ Value Index (R25IV) returned 1.89%, though only six of 11 economic sectors ended the quarter in positive territory.

Portfolio Performance & Developments

Cooke & Bieler's SMID Cap Value Strategy returned 5.83% gross of fees (5.59% net of fees), handily beating the R25IV and building on its healthy Q1 outperformance. Favorable stock selection effect accounted for approximately half of the excess return in Q2, with notably strong relative results in the Consumer Discretionary sector. Stock selection was also favorable in the Financials sector, with modest drags coming from positions within Information Technology and Health Care.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Winnebago	4.5	24.9	104
Steelcase	2.6	18.5	43
PGT Innovations	2.2	20.7	42
FirstCash	2.5	15.9	40
FNF Inc.	3.3	11.1	37

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Schweitzer-Mauduit	3.0	-13.1	-44
Gates	1.8	-20.4	-39
Arrow Electronics	3.2	-7.5	-23
Varex Imaging	1.9	-9.5	-19
Rush Enterprises	1.2	-12.4	-17

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.

Largest Contributors

Winnebago Industries (WGO), a leading designer and manufacturer of recreational vehicles, was the largest contributor this quarter. Fundamental performance within WGO's towable division continues to buck industry trends. Though industry-level concerns persist, investors seem to be warming to the company's long-term topline growth and margin expansion opportunities.

Steelcase (SCS), one of the world's leading manufacturers of office furniture, was the second-largest contributor. SCS advanced amidst encouraging fundamental signs that the company is competing effectively and taking advantage of strong demand tied to favorable workspace modernization trends.

PGT Innovations (PGTI), a specialty window manufacturer, was the third-largest contributor. PGTI's organic results were solid thanks to robust new construction growth and despite difficult hurricane-driven comparisons in its renovation and remodel business. In addition, its Western Window Systems acquisition performed better than expected, as market share gains offset weak industry dynamics in California.

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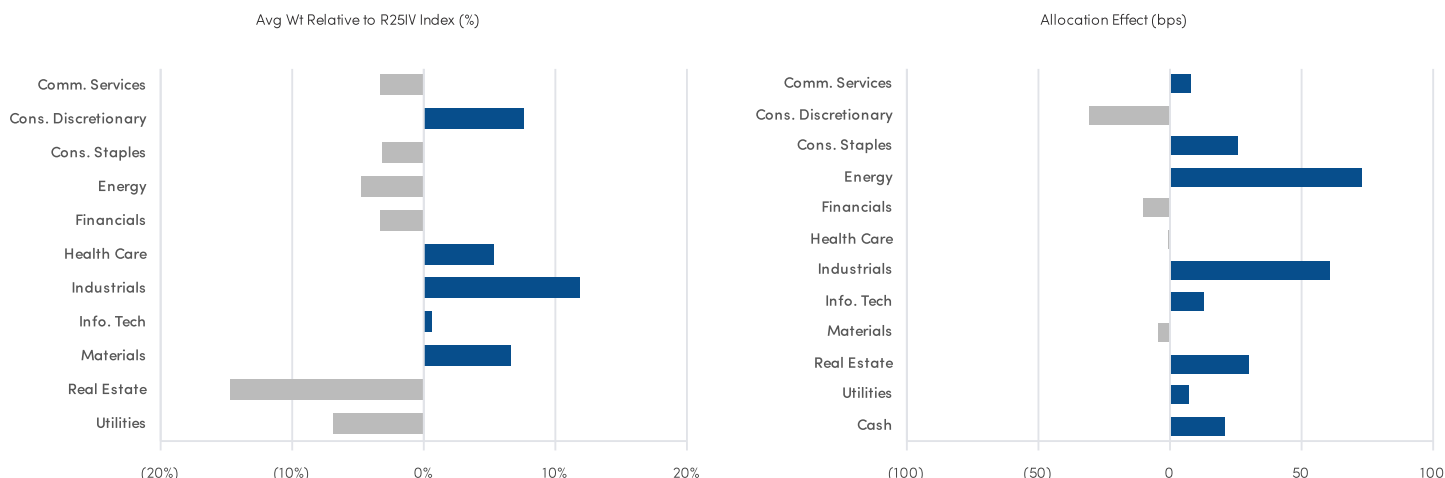
Largest Detractors

Schweitzer-Mauduit International (SWM), an advanced materials and engineered solutions provider, was the largest detractor this quarter. SWM was a top performer last quarter and this quarter's underperformance partially reflected a reversal of investor enthusiasm. Some fundamental volatility in reported results has investors more cautious on management's targets for the full year.

Gates (GTES), a global manufacturer of premium transmission belt and fluid power products, was the second-largest detractor. Roughly two-thirds of GTES' sales are to the more recurring and higher margin replacement channel, which experienced softness in the quarter related to unexpected inventory destocking. This, and more expected weakness in European and Chinese first fit sales in automotive end markets, led to disappointing quarterly results and lowered full-year guidance. Despite this setback, GTES' exposure to the replacement channel should serve to stabilize results over the long term while attractive organic and inorganic growth opportunities combined with an improving free cash flow profile provide attractive upside potential.

Arrow Electronics (ARW), a solutions provider for users of electronic components and enterprise computing, was the third-largest detractor. Although ARW previously had good operating income growth and margin expansion, progress reverted during this quarter. Concerns about general levels of tech spending as well as elevated inventories in the semiconductor components supply chain also negatively affected ARW's performance this quarter.

Sector Positioning



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.

Sector allocations explained approximately half of the strategy's second quarter outperformance. The largest contributors were the portfolio's meaningful underweight in Energy and Real Estate, as well as an overweight in Industrials – the R25IV's best performing sector for the quarter. This impact was partially offset by the negative effects of the portfolio's overweight in the Consumer Discretionary sector and underweight in Financials. Exiting the quarter, the strategy remains underweight the high-yielding Real Estate and Utilities sectors and broadly overweight economically sensitive sectors including Consumer Discretionary and Industrials. Energy continues to be a significant underweight and partial offset to the portfolio's pro-cyclical tilt.

Initiations

American Eagle Outfitters (AEO) is a teen and young adult retailer operating under two brands: American Eagle and Aerie. Aerie is a women's innerwear concept that appears well positioned for long-term growth. AEO's valuation does not accurately incorporate this potential, and investor concern surrounding China trade tension gave us the opportunity to initiate a position.

MKS Instruments (MKSI) supplies components and subsystems to companies in the semiconductor capital equipment industry, among others. MKSI's growth strategy of adding more content per customer system as well as expanding into adjacent markets has proven effective. Recent concerns about the level of semiconductor capital equipment spending created a buying opportunity.



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Eliminations

Fox Factory (FOXF) was eliminated after reaching its price target. **MTS Systems (MTSC)** and **RenaissanceRe (RNR)** were eliminated to make room for better opportunities.

Outlook

Bumpy quarters like Q2 tend to reinforce investors' short-term focus. But rather than try to guess the next twist in the market, we find it more profitable to look to the long term and focus on fundamentals. Taking the long view, over the last 15 years – a period that saw two oil price spikes, a global financial crisis, unprecedented monetary intervention, and countless political shocks – the R25IV has generated a fairly typical 8.1% annualized return. In other words, the confusion and cross currents of the second quarter are par for the course, presenting an opportunity to profit from others' impatience rather than a cause for alarm for long-term oriented investors. From a fundamental standpoint, the business environment remains mostly positive, albeit with pockets of weakness emerging as trade tensions begin to take their toll. Valuations, broadly speaking, seem fair – neither compellingly cheap, nor worryingly expensive. This combination leads us to believe returns will be volatile, but positive over time. We remain confident that our long-term approach and disciplined focus on fundamentals, balance sheets, and valuation are well suited to profit both from the opportunities created by volatility as well as the long-term compounding ability of quality businesses.

Sources: Bloomberg; FactSet; FTSE Russell; Market Watch; The New York Times; T. Rowe Price

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 6/30/19. 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 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.

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