Reinhart Partners, Inc.

PMV March 2018 Quarterly Review

After a year of ever-higher stock prices in the momentum-led market of 2017, U.S. equities experienced the return of volatility in the first quarter of 2018. The often quoted VIX (CBOE Volatility Index) doubled from 10 to 20 during Q1. Markets suddenly seemed aware of their own elevated valuations and investors grew skeptical over how much longer this nine year bull market might last. As a result, major equity indices declined during Q1 for the first time in ten quarters (going back to Q3'15), and risk aversion among market participants returned to what we consider healthier levels.

In this volatile environment, the Mid Cap Private Market Value ("PMV") portfolio thrived by generating positive absolute returns for the quarter, and gross performance outpaced the Russell Midcap Value Index. As our long-term clients have come to expect, PMV was able to weather the storm by taking advantage of volatility and mean reversion within the mid cap universe. Reinhart also benefited from many strong Q4 EPS reports and forward guidance, as our companies raised their annual 2018 EPS forecasts by an average of 8% since year-end. Granted much of these gains came from corporate tax reform, which we believe will benefit many of our holdings due to their high percentage of profits in the U.S. Furthermore, our analysis suggests that only those firms with pricing power and strong competitive advantages will retain these tax savings in the face of competition, and we believe PMV has a healthy dose of just such companies.

Looking at portfolio attribution during Q1, over 90% of the alpha came from bottom-up stock selection, a pattern we've seen many times before. The positive performance was broad-based with strength from holdings within Real Estate, Technology, Health Care and Consumer Discretionary. Our research conviction and patience paid off, as 11 of 41 portfolio holdings generated double-digit returns during Q1, many of which had previously lagged the market during 2017. The only area of significant weakness came within Energy, which cost PMV approximately -40bps during the quarter on a relative basis.

Looking forward, we would highlight three significant conclusions from our research process:

- Market volatility may be here to stay for a while given still high equity valuations, tightening monetary policy, and geopolitical risks.
- Value stocks have lagged growth significantly (~1500bps in the mid cap universe since 12/31/16) and appear more reasonably valued going forward.
- Corporate profit margins may peak in 2018, as tax benefits wane and higher wages, transportation and material costs weigh on profits.

Overall we are happy to report the portfolio was able to widen its average discount to our PMV estimates from 19% at year-end to 22% in Q1. This valuation improvement came from better company fundamentals, the reallocation of capital within the portfolio and our overall sell discipline. As we follow through on the PMV process and work to reduce risk within the portfolio, we are reminded of a recent quote from Warren Buffett in his February letter to shareholders.

"The less prudence with which other investors conduct their affairs,
the greater the prudence with which we must conduct our own."

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Chicago Board Options Exchange Volatility Index (VIX): an unmanaged index calculated from options on the S&P 500 Index and is supposed to reflect the market expectation of the index's annualized 30-day volatility. The volatility measured by the VIX reflects both the possibility of upside movements as well as the possibility of downside movements. An investment cannot be made directly to an index.

Russell Midcap Value Index: an unmanaged index that measures the performance of those Russell Midcap companies with lower price-to-book ratios and lower forecasted growth values. An investment cannot be made directly to an index.