

**MARKET COMMENTARY**

The Russell 2000 Index declined -4.4% in the third quarter of 2021, underperforming large caps which were slightly positive. Economic developments over the quarter were mixed. Real GDP grew an impressive +6.7% in the most recent quarter (seasonally adjusted quarter-over-quarter). The positive momentum in labor markets slowed, however, as many businesses are contending with serious labor shortages. Business owners are hopeful that labor availability will improve due to the expiration of enhanced pandemic unemployment benefits in September, though higher wages and benefits appear likely. This fuels already-tight supply conditions and increases inflationary pressures. Inflation persisted above 5% (year-over-year), its highest level in well over a decade. The Fed voted to keep its target Fed Funds rate near zero until the economy approaches “maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time.”<sup>1</sup> There have been some increasingly hawkish comments from Federal Open Market Committee (FOMC) members, with some suggesting that the economic recovery warrants tapering in the near term. The yield on the 10-year treasury note began and ended the quarter at about 1.5% but fell below 1.2% intra-quarter. Shorter and longer duration treasuries experienced similar moves during the quarter, i.e., there was little change to the yield curve.

Oil prices followed a curiously similar path to interest rates. WTI crude oil began the quarter at about \$73/barrel, then declined to nearly \$62/barrel intra-quarter, before reverting to \$75/barrel by quarter end. Through July and August, energy stocks in the Russell 2000 were down more than -12%, the worst performing sector in the index. This reversed in September. All Russell 2000 sectors declined during September except energy, which was up more than +16% as crude prices rose. For the entire quarter, energy was one of two sectors with a positive return, though it was modest rise (+1.9%). Financials were the other positive group, as banks, consumer finance, and capital markets companies outperformed. Communication services performed worst, largely due to the decline in meme stock AMC Entertainment. Overall, Corporate America continues to perform well as nearly two-thirds of Russell 2000 companies surpassed consensus earnings expectations in the quarter.

Small value outperformed (declined less than) small growth. The Russell 2000 Growth Index declined -5.7% while the Russell 2000 Value Index declined -3.0%. In the recent past, COVID-19 developments appear to have dictated which investing style outperformed—positive developments have favored value,

negative developments growth. At the beginning of the year, there were more than 200,000 new confirmed cases per day in the US<sup>2</sup>. Accordingly, the Russell 2000 Growth outperformed the Russell 2000 Value in the first month and a half of 2021. As cases fell and persisted around or below 100,000/day, small value outperformed considerably. Year-to-date through September, the Russell 2000 Value outperformed the Russell 2000 Growth by more than 20 percentage points (+22.9% vs. +2.8%). We continue to focus on fundamentals and valuation because that is what drives stock prices in the long run; however, we believe the demise of the pandemic through improved inoculation, herd immunity, or both, could provide a welcomed catalyst for a prolonged value rally.

Dating back to 1926, the average value rally has lasted just shy of three years, with an average outperformance of 55 percentage points, cumulatively<sup>3</sup>. Some of the more powerful and long-lasting value rallies have persisted for 7 to 10 years, with value outperforming growth by well over 100 percentage points. Taking a deeper look into these rallies, we observe important similarities between today's environment and the early stages of the strongest and longest value rallies. Specifically, the best value led markets came on the heels of a prolonged period of growth outperformance, and each began with wide valuation spreads. Today, value stocks are coming out of one of the worst periods of underperformance since 1926 and are starting from one of the deepest valuation discounts on record. We see a value-led market being a strong tailwind to our investment approach.

**ATTRIBUTION – 3Q21**

The Hotchkis & Wiley Small Cap Diversified Value Fund outperformed the Russell 2000 Value Index in the third quarter. The overweight position and positive stock selection in financials helped relative performance in the quarter. The underweight and positive stock selection in communication services also helped, though this was largely a function of not owning meme stock AMC Entertainment, which lost one-third of its market value. Positive stock selection in consumer discretionary and technology also contributed to the outperformance. Stock selection in energy, healthcare, and industrials, along with the overweight position in consumer discretionary and underweight position in real estate, detracted from performance.

<sup>1</sup> <https://www.federalreserve.gov/monetarypolicy/files/monetary20210922a1.pdf>

<sup>2</sup> 7-day moving averages

<sup>3</sup> Statistics in this paragraph reference data from the Kenneth French Dartmouth data library

Portfolio managers' opinions and data included in this commentary are as of September 30, 2021 and are subject to change without notice. Any forecasts made cannot be guaranteed. Information obtained from independent sources is considered reliable, but H&W cannot guarantee its accuracy or completeness. Fund holdings and/or sector allocations are subject to change and are not buy/sell recommendations. Current and future portfolio holdings are subject to risk. Certain information presented based on proprietary or third-party estimates are subject to change and cannot be guaranteed. **Diversification does not assure a profit nor protect against loss in a declining market. Past performance is no guarantee of future results.**



# SMALL CAP DIVERSIFIED VALUE FUND

HWVIX  
HWVAX  
HWVZX

## MANAGER REVIEW & ECONOMIC OUTLOOK

SEPTEMBER 30, 2021

### PERFORMANCE (%) as of September 30, 2021

	QTR	YTD	1 Yr	3 Yr	5 Yr	Since 6/30/14
Small Cap Diversified Value Fund – I Shares	-1.29	27.87	75.84	7.96	12.18	9.43
Russell 2000 Value	-2.98	22.92	63.92	8.58	11.03	8.47

*The performance shown represents past performance. Past performance is no guarantee of future results and current performance may be higher or lower than the performance shown. Investment results and principal value will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. To obtain performance data current to the most recent month-end, access our website at [www.hwcm.com](http://www.hwcm.com).*

The Fund's total annual operating gross expense ratio as of the most current prospectus is 0.87% for I Shares; 0.80% net expense ratio. The Advisor has contractually agreed to waive advisory fees and/or reimburse expenses through August 31, 2022. Expense ratio shown is gross of any fee waivers or expense reimbursements. I Shares sold to a limited group of investors. Periods over one year are average annual total return. Average annual total returns include reinvestment of dividends and capital gains. Expense limitations may have increased the Fund's total return.

*You should consider the Fund's investment objectives, risks, and charges and expenses carefully before you invest. This and other important information is contained in the Fund's summary prospectus and prospectus, which can be obtained by calling 1-800-796-5606 or visiting our website at [www.hwcm.com](http://www.hwcm.com). Read carefully before you invest.*

*Investing in smaller and/or newer companies involves greater risks than those associated with investing in larger companies. Please read the fund prospectus for a full list of fund risks.*

Equities, bonds, and other asset classes have different risk profiles, which should be considered when investing. All investments contain risk and may lose value. Attribution is an analysis of the portfolio's return relative to a selected benchmark, is calculated using daily holdings information and does not reflect the payment of transaction costs, fees and expenses of the Fund.

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**Style Risk:** A value-oriented investment approach involves the risk that value stocks may remain undervalued or may not appreciate in value as anticipated. Value stocks can perform differently from the market as a whole or from other types of stocks and may be out of favor with investors and underperform growth stocks for varying periods of time.

**Market Disruption:** The global coronavirus pandemic has caused disruption in the global economy, unprecedented business and travel disruption and extreme fluctuations in global capital and financial markets. H&W is unable to predict the consequences of the upheaval caused by coronavirus pandemic, which has the potential to negatively impact the firm's investment strategies and investment opportunities.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The Russell 2000® Value Index measures the performance of those Russell 2000® companies with lower price-to-book ratios and lower forecasted growth values. The Russell 2000® Growth Index measures the performance of those Russell 2000® Index companies with higher price-to-book ratios and higher forecasted growth values. The indices do not reflect the payment of transaction costs, fees and expenses associated with an investment in the Fund. It is not possible to invest directly in an index. Top ten holdings as of 9/30/21 as a % of the Fund's net assets: Penn Virginia Corp. 0.6%, Range Resources Corp. 0.6%, California Resources Corp. 0.5%, Whiting Petroleum Corp. 0.5%, Kosmos Energy Ltd. 0.5%, Bonanza Creek Energy Inc. 0.5%, Northern Oil and Gas Inc. 0.5%, PDC Energy Inc. 0.5%, Oasis Petroleum Inc. 0.5%, and Nextier Oilfield Solutions Inc. 0.5%.

Duration is a measure of the price sensitivity of a bond to interest rate movements. Yield curve is a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. Spread is the difference between valuations of value and growth stocks. **Extraordinary performance is attributable in part due to unusually favorable market conditions and may not be repeated or consistently achieved in the future.**

Mutual fund investing involves risk. Principal loss is possible.  
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