Westwood®

Westwood **Quality SmallCap Fund (WHGSX)**

Commentary

1Q
2024

Performance Highlights

- In a challenging market for small-cap stocks, the Westwood Quality SmallCap Fund outperformed its benchmark index. The Fund gained 3.81% in the quarter, compared to a 2.90% gain for the Russell 2000 Value Index.
- The small-cap market managed to move higher on improving economic conditions by many metrics. Large-cap stocks — especially those involved with artificial intelligence (AI) — led performance in the broad market. Investors were still apt to reward smaller companies for better-than-expected earnings growth, despite what seems to be an increasingly challenged, yet resilient consumer. Investors favored growth over value in the quarter, as risk appetite remained strong.
- Both asset allocation and security selection were positive factors in the quarter. The top contributors to relative performance were the **Industrials** and **Financials** sectors, while **Health Care**, **Consumer Discretionary** and **Consumer Staples** sectors were relative detractors.
- Security selection was a key positive factor in the Industrials sector, helped along by a merger among our top holdings. Our selections in the Financials sector were also a positive contributor, as our holdings handily outperformed the benchmark. Our underweight position in Financials was also beneficial, as was the overweight to Industrials.
- Two medical device companies were key detractors, impacting relative performance of the Health Care sector. Selection was also a detractor in the Consumer Discretionary sector, as a pair of restaurants detracted from performance.

Performance Drivers

- On an absolute return basis, the **Energy** sector was the best performer in the quarter, while the top contributor to absolute performance was **Industrials**, due to a combination of a large weight in the portfolio and strong absolute returns. Our **Communication Services** position was the worst performer on an absolute basis, while **Real Estate** detracted the most from an absolute basis when sector sizing is included.
- The top-performing position in the portfolio was **Masonite International Corp. (DOOR)**, which soared over 50% after agreeing to be acquired by Owens Corning. We exited the position as our investment thesis became fully realized. Another takeout was **Enerplus Corp. (ERF)**, which agreed to be purchased by Chord Energy for a significant premium.
- **Blue Bird Corp. (BLBD)** gained over 50% in the quarter; the school bus manufacturer advanced on strong earnings and prospects for future growth. Insurer **BRP Group (BRP)** advanced smartly after a tough fourth quarter 2023; the company provided guidance ahead of Street expectations and posted strong fourth quarter revenues. **SM Energy Corp. (SM)** gained nearly 30% on a positive earnings surprise and guidance that pleased analysts.
- The top detractor from performance in the quarter was **CONMED Corp. (CMED)**, which fell after reporting earnings below Street expectations and lower guidance for future revenues. **J&J Snack Foods Corp. (JNJ)** fell as investors became more cautious on consumer spending. **Papa John's International (PZZA)** declined as management cited higher expenses and potentially slowing consumer spending; also, the company's CEO unexpectedly announced he was leaving to take the reins at Shake Shack.
- **Seacoast Banking Corp. of Florida (SBCF)** was among the top decliners as regional banks had a tough run in the first quarter; higher interest rates have caused analysts to scrutinize balance sheets. Finally, **Mercury**

Systems Inc. (MRCY) declined after another messy quarter where they fell short of revenue targets and lowered guidance but cleared up their development pipeline and showed some growth in future bookings.

Performance Update

As of March 31, 2024

Trailing Years Performance

	1Q24	YTD	1 Year	3 Year*	5 Year*	10 Year*	Since Inception*
Westwood Quality SmallCap Fund	3.81%	3.81%	18.26%	5.22%	9.08%	8.07%	7.97%
Russell 2000 Value Index	2.90%	2.90%	18.75%	2.22%	8.17%	6.87%	6.26%

*Annualized

Calendar Year Returns

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Westwood Quality SmallCap Fund	-32.11%	20.42%	23.23%	-1.40%	18.13%	49.39%	6.05%	-5.94%	28.33%	12.36%	-14.16%	27.13%	2.16%	27.93%	-12.46%	17.17%
Russell 2000 Value Index	-28.92%	20.58%	24.50%	-5.50%	18.05%	34.52%	4.22%	-7.47%	31.74%	7.84%	-12.86%	22.39%	4.63%	28.27%	-14.48%	14.65%

Inception date is 4/2/2007. High short-term performance of the fund is unusual and investors should not expect such performance to be repeated. **The performance data quoted represents past performance. Past performance is not indicative of future results. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. For performance data current to the most recent month end, please call 877.FUND.WHG.** Expense ratio for the fund is 1.04% (gross) and 0.92% (net). The Advisor has contractually agreed to waive fees and reimburse expense until March 1, 2024. In the absence of current fee waivers total return and yield would be reduced.

Potential Risks

Mutual fund investing involves risk, including possible loss of principal. There can be no assurance that the Fund will achieve its stated objectives. There are specific risks inherent in small cap investing such as greater share price volatility as compared to other funds that invest in stocks of companies with larger and potentially more stable market capitalizations.

Top 10 Holdings as of 3/31/2024

Blue Bird Corp.	Atlantic Union Bankshares Corp.
CONMED Corp.	SM Energy Co.
GMS Inc.	Triumph Financial Inc.
Avista Corp.	Renasant Corp.
Merit Medical Systems Inc.	PotlatchDeltic Corp.

Top 10 Holdings represents 20.66% of the total portfolio and represents the ten largest portfolio positions by market value in the Fund as of the period end date. Each quarter, The Westwood Funds use this same objective, non-performance based criteria to select the ten largest holdings. Holdings are subject to change. Current and future portfolio holdings are subject to risk.

Fund Positioning and Trade Rationale

Positions were initiated in the following companies:

- **Blue Bird Corporation (BLBD):** The school bus manufacturer was added to the portfolio based on an elevated backlog, providing a clear line of sight to future revenue streams. The company also manufactures EV buses, with support of a $5 billion EPA program, another potential growth driver.
- **GMS, Inc. (GMS):** The company makes building products, including wallboard, steel framing, ceilings and other similar products. The pricing environment for wallboard is resilient, and there seems to be a recovery in new residential building, which increases demand for the company's products.
- **Hawkins, Inc. (HWKN):** Hawkins is a specialty chemical company that offers water treatment, industrial and health care products. The company's water treatment products are underappreciated by the market, as there is increasing demand for clean drinking water driven by stringent EPA regulations and ongoing infrastructure development.
- **Kratos Solutions, Inc. (KTOS):** A defense contractor with a focus on drones, software, electronic warfare and propulsion, the company is well-positioned to take advantage of the Defense Department's future investment and spending plans.
- **Simmons First National (SFNC):** Simmons Bank, headquartered in Little Rock, Arkansas, operates in six states, including Texas. Under new leadership, the bank has focused on organic growth, efficiency and profitability. The bank is materially under-earning its potential due to poor balance sheet construction, which we believe will be fixed soon. As the bank takes steps toward cleaning up its operations, we believe the market will reward it with higher valuation multiples.
- **Thermon Group Holdings, Inc. (THR):** Thermon is a global leader in industrial heating and has consistently generated high margins largely due to the oligopolistic nature of the heat tracing business and its supply of critical products to large industrial projects. The company has diversified its client base toward higher-margin opportunities, including projects for decarbonization and energy transition. The company is under-covered by Wall Street, which has resulted in an attractive valuation.
- **Verra Mobility (VRRM):** The software company designs and develops solutions for toll management, safety and traffic enforcement. There are opportunities for growth as highly populated states such as California, Florida and Pennsylvania have passed legislation, creating opportunities for growth in their Government Solutions business, while there are additional opportunities in tolling with the shift to cashless toll roads.

The following positions were sold from the portfolio:

- **Comfort Systems USA (FIX):** We sold the stock in Comfort Systems, a long-time holding in our portfolio, as it moved outside of our target market capitalization range.
- **Easterly Government Properties (DEA):** The stock of this REIT focusing on government properties was sold to reduce our exposure to real estate.
- **Encore Wire Corp. (WIRE):** Another long-term holding, the stock had gained significant ground, and the reward to risk ratio became less favorable.
- **Federal Signal Corp. (FSS):** The stock gained over 200% since we initially purchased it in 2019; we believe the investment thesis has come to fruition.
- **Masonite International Corp**. **(DOOR):** The company agreed to be purchased by Owens Corning for a 38% premium to its close on Feb. 8; we exited the position following the news.
- **Monro Inc. (MNRO):** We sold the position based on a broken investment thesis and concerns about execution and potential market share.
- **Provident Financial Services (PFS):** We sold the position to help fund the purchase of a different bank that we believe is better positioned for growth and stock price appreciation.
- **Summit Materials (SUM):** We sold our position in this building materials provider after a run of strong performance pushed the market capitalization outside of our target range.

Market Review

Equity markets experienced overall growth in the first quarter of 2024, with both the Dow Jones Industrial Average and the S&P 500 setting record highs in the quarter. The closely watched S&P 500 returned 10.6%, marking the second quarter in a row of double-digit gains and reaching a new high of 5,245 in March. Broad-based market optimism, confidence in corporate earnings and any “landing” still to come in the economy fueled those markets. Large-cap stocks continued to outpace small-cap issues, though small- and mid-cap stocks enjoyed a strong March. From a style perspective, growth outperformed value over the entire market cap spectrum.

Bond markets trended sideways to lower as resilient economic data and sticky inflation prompted a revival in the “higher for longer” interest rate case that was confirmed by the Federal Reserve in their March meeting. Despite the shift in the Fed’s sentiment, investors continued to believe in a benign risk environment.

Technology stocks performed well, driven by increased demand for digital services and the positive outlook on innovation, technology adoption, and AI. Energy was the second-best-performing equity sector in the quarter, as concerns over the Middle East conflict kept oil and natural gas prices high. The Financials and Industrials sectors also saw significant gains, buoyed by the broader economic recovery and increased infrastructure spending.

The Magnificent 7 led the way for all stocks as AI remained a tremendous catalyst for earnings growth across a myriad of stocks and sectors. The Magnificent 7 were responsible for 40% of the S&P 500’s year-to-date gain, compared to more than 60% last year.

The bond market was not as bullish as we saw late last year, but showed signs of stabilization, with yields on government bonds remaining relatively steady. The 10-year Treasury yield, a key indicator for borrowing costs, closed the quarter at 4.20%, up from its final read in 2023 of 3.88%. The decline in the Treasury bond market reflects the Federal Reserve’s cautious approach to interest rate cuts, now expected to total just three for the rest of the year, less than half of what was expected in early January. Corporate bond yields, on the other hand, experienced a slight increase, reflecting the improved credit outlook for many companies and the overall optimism in the market.

In the U.S. economy, the first quarter saw a significant uptick in job creation, as over 1.5 million jobs were added across various sectors, most notably in technology, health care and manufacturing. This level of job creation points to a resilient and adaptable economy. On the other hand, there were an increasing number of layoffs and cost-cutting actions by companies large and small. Nearly 40% of business leaders surveyed by ResumeBuilder believe layoffs are likely at their companies this year, and about half say their companies will implement a hiring freeze.

Consumer spending remained strong in January and February, indicating relative confidence among the American public, with a notable increase in spending on durable goods. The housing market experienced a slowdown in price appreciation, suggesting a shift toward a more balanced market, though demand for housing remained healthy. Low-rate mortgage owners are staying put, restricting supply for now.

Global economic recovery efforts, particularly in major trading partners like the EU and China, have positively influenced American exports, contributing to the growth in manufacturing jobs and sectors reliant on international trade, but the relative economic health of many of our trading partners remains delicate. Recessions are occurring in the U.K., Finland and Ireland, and negative GDP rates for Q4 2023 were also reported in Germany and Canada.

International stocks are positive on the year but are also showing divergence across regions and countries. The MSCI ACWI ex-U.S. Index was up 4.3% in the quarter, while the MSCI Emerging Markets Index gained 2.2%. Within developed international markets, Japan was certainly a standout, despite economic fragility and rising interest rates. Japan’s Nikkei 225 recaptured a high last made 35 years ago as the Bank of Japan increased its short-term borrowing rate for the first time in 17 years. Japanese companies continue to benefit from corporate reforms and a very weak yen, weighed by years of easing monetary policy.

Outlook

We continue to maintain a cautiously optimistic outlook for both stocks and bonds for the coming year. While not as dovish as many might have hoped, the Fed should begin lowering rates at a slow pace around mid- to late-year as long as inflationary pressures remain in check. The jury is still out on two or three cuts this year; we are leaning more toward the former.

Headline consumer data still suggests optimism, but we remain concerned about housing costs, depleted savings and record high-rate credit card debt. And while easing inflation is good for consumers, it reduces pricing power and margin growth for companies. Earnings growth should continue to accelerate into 2024, assuming lower rates into the back half of the year.

We are most concerned about the health of the labor market, and how that impacts consumer spending, particularly among lower-income households, which appear to be holding back. We are also cognizant of geopolitical pressures, as well as ongoing government dysfunction in Washington D.C., as we head into a contentious political season.

We remain excited about the undervalued quality and resilient earnings power in the companies in our portfolio. While we carefully monitor holdings and actively manage risk, we believe we are positioned appropriately given the elevated uncertainty in the economy and the markets.

Important Information

To determine if this Fund is an appropriate investment for you, carefully consider the Fund's investment objectives, risk factors, charges and expenses before investing. This and other information can be found in the Fund's summary or full prospectus, which may be obtained by calling 1.877.FUND.WHG (877-386-3944), or by visiting our website at westwoodfunds.com. Read the prospectus carefully before investing or sending money.

The Russell 2000® Value Index measures the performance of those Russell 2000® Index companies with lower price-to-book ratios and lower forecasted growth values. The Benchmark Index returns are for illustrative purposes only and do not represent actual fund performance. Index performance does not reflect any management fees, transaction costs or expenses. The Benchmark Index is unmanaged and investors cannot invest directly into an index. The S&P 500® Index is a capitalization weighted unmanaged index of 500 widely traded stocks, created by Standard & Poor's. The index is considered to represent the performance of the stock market in general. VIX is the ticker symbol and the popular name for the Chicago Board Options Exchange's CBOE Volatility Index, a popular measure of the stock market's expectation of volatility based on S&P 500 index options.Growth is a term used to refer to a share in a company that is anticipated to grow at a rate significantly above the average for the market. Value is a term used to refer to a company that tends to trade at a lower price relative to its fundamentals, such as dividends, earnings and sales, making them appealing to value investors. Small cap is a term used to refer to a company with a market capitalization between $300 million and $2 billion. A company's market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share. Meme stocks is a stock that has seen an increase in volume not because of how well the company performs, but rather because of hype on social media and online forums.

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