



# Small Cap Value Equity Strategy Update

Composite Inception Date is 7/1/2012	QTR	YTD	1 YR	3 YR	5 YR	Since Inc.
Small Cap Value Equity (Gross)	5.79%	7.82%	22.32%	14.80%	17.03%	17.23%
Small Cap Value Equity (Net)	5.53%	7.01%	21.10%	13.66%	15.93%	16.18%
Russell 2000 Value Index	5.11%	5.68%	20.55%	12.12%	13.27%	13.78%

## Market Recap

The US economic growth acceleration that began in the middle of last year has largely continued through the third quarter. US second quarter GDP came in at a fairly strong 3.0% – the best reading since 1Q15. In addition, the Purchasing Managers Index (PMI) manufacturing data for August provided further support for a strengthening economy. The positive surge in softer sentiment measures such as consumer confidence has continued to improve with recent employment growth. The same has been true for business sentiment indicators as a more pro-business regulatory environment has further boosted confidence. However, the destruction caused by Hurricanes Harvey and Irma will likely diminish third quarter GDP since economic output and demand are both impeded, yet historically, these moves are usually quickly reversed.

## Strategy Overview

The RBC Small Cap Value Equity strategy is moderately underweight to the benchmark's health care and real estate weightings, is significantly overweight to industrials, moderately overweight materials, and has no holdings in the tiny telecom services sector.

Favorable stock selection drove returns primarily within the information technology (+92 bps) and materials (+29 bps) sectors. However, this was modestly offset by adverse stock selection within the health care (-38 bps) and consumer staples (-29 bps) sectors. Overall, the strategy's sector allocation decisions contributed slightly to returns with a significant overweight to the strong performing industrials sector boosting performance, though the residual cash weighting was a drag on returns.

## Strengths

- **Columbus McKinnon Corp.** (+0.62%): *Manufactures material handling products*; Earnings far exceeded expectations driven by strong US industrial demand for hoists and other lifting machinery, good results from recent acquisition, and implementation of more efficient operating system.
- **Novanta, Inc.** (+0.38%): *Manufactures and sells laser based solutions and precision motion and optical control technologies*; Delivered record quarter with strong double-digit revenue and earnings growth. Closed on its acquisition of World of Medicine, giving them more exposure to medical end markets.
- **Take-Two Interactive Software, Inc.** (+0.36%): *Video game developer*; Significantly beat earnings expectations driven by Grand Theft Auto and its online incarnation, which both performed better than anticipated. Digital revenue overall was up 47%.
- **Koppers Holdings, Inc.** (+0.34%): *Global chemical and materials company*; Beat earnings estimates driven by the Carbon Materials and Chemicals segment, which increased due to higher volumes and pricing for carbon pitch and carbon black feedstock. Benefitted from restructuring initiatives and lower raw material and logistics costs.

- **Vishay Precision Group, Inc.** (+0.32%): *Leading producer of precision sensors and systems*; Continues to benefit from successful restructuring and improved business climate. Foil Technology Products segment revenues grew 15.6%.

## Weaknesses

- **Spirit Airlines, Inc.** (-0.45%): *Ultra low cost airline*; Shares were under significant pressure due to fare discounting from competitors in core markets and Spirit's upcoming new pilot agreement that could increase costs.
- **Dean Foods Co.** (-0.35%): *Food and beverage company and the largest dairy company in the US*; Missed earnings estimates and slashed guidance by 40% reflecting weaker than expected volume, inflationary milk pressures, and weaker mix performance (branded vs. private label).
- **American Outdoor Brands Corp.** (-0.34%): *Firearm and outdoor sports and recreation products manufacturer*; Results hurt by high inventory levels and limited sell-through of firearms at retailers, which limited near-term orders. Revenue also faced a challenging comparison to last year's heightened level of demand.
- **Synaptics, Inc.** (-0.17%): *Makes computer hardware such as display controllers, touchpads, etc.*; Guided down given greater competition in its biometrics products and fall-off in its discrete display driver business. Weaker fingerprint sensor pricing, the impact of Apple's move to OLED, and slower touch and display driver integration were the main culprits.
- **Globus Medical, Inc.** (-0.14%): *Medical device company*; Weakness in volumes across spine companies in general and some profit taking after a run up in med-tech industry. Globus also reported a slight delay in their upcoming growth drivers.

## Outlook

The RBC Small Cap Value Equity strategy focuses on neglected small cap companies with attractive long-term fundamentals, near-term profitability improvement potential, and low relative valuations. The strategy emphasizes market leaders with proven products or services, sustainable competitive advantages, solid balance sheets, and attractive cash flows. While sector weightings are a result of bottom-up research and stock selection, the strategy remains positioned for economic recovery with overweight positions in the economically sensitive industrials, materials, and consumer discretionary sectors. Downside protection is provided by the superior return on equity and balance sheet profile of the portfolio compared to the index and the market leadership positions of most portfolio companies. The strategy continues to trade at a valuation discount to the Russell 2000 Value Index on several measures while providing superior projected earnings growth and return on equity.

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**Past performance is not indicative of future results.**

Returns include the reinvestment of all income. All returns for periods greater than one year are shown on an annualized basis.

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## GIPS® Compliant Presentation as of September 30, 2017

Year	Composite Return Gross of Fees	Composite Return Net of Fees	Benchmark Return	# of Portfolios	Composite Dispersion	Composite 3-Year Standard Deviation	Benchmark 3-Year Standard Deviation	Composite Assets	Total Firm Assets
2012 <sup>1</sup>	10.19%	10.19%	9.07%	1	N/A <sup>2</sup>	N/A <sup>2</sup>	N/A <sup>2</sup>	\$0.6M	\$279,416.3M
2013	33.09	31.76	34.52	1	N/A <sup>2</sup>	N/A <sup>2</sup>	N/A <sup>2</sup>	0.7	296,003.0
2014	12.36	11.24	4.22	1	N/A <sup>2</sup>	N/A <sup>2</sup>	N/A <sup>2</sup>	0.8	302,064.4
2015	-1.58	-2.56	-7.47	4	N/A <sup>2</sup>	11.80%	13.46%	136.1	276,979.3
2016	31.78	30.47	31.74	4	1.22%	14.11	15.50	217.4	289,538.6
YTD 2017	7.82	7.01	5.68	6	0.22	13.54	14.37	381.0	319,111.8

<sup>1</sup>Performance calculated from 7.1.12 to 12.31.12

<sup>2</sup>N/A – Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

**Description of the Firm:** For the purposes of Global Investment Performance Standards (GIPS®), RBC Global Asset Management is the asset management division of Royal Bank of Canada (RBC), operating under the following brands: RBC Global Asset Management (RBC GAM) in Canada, the U.S. (institutional), the U.K. and Hong Kong; Phillips, Hager & North Investment Management (institutional); and BlueBay Asset Management (institutional). With offices around the world, RBC GAM offers a full range of global investment solutions in cash management and fixed income, equity, balanced, alternative and specialty investment strategies through mutual funds, hedge funds, pooled funds and separately managed accounts. The RBC GAM group of companies has more than C\$388 billion (US\$289 billion) in assets under management as at December 31, 2016. RBC purchased Phillips, Hager & North Investment Management, including the assets of BonaVista Asset Management, on May 1, 2008, and BlueBay Asset Management on December 17, 2010. A complete list and description of the firm's composites and performance results is available upon request.

**Compliance Statement:** RBC GAM claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. RBC GAM has been independently verified for the periods January 1, 2002 through December 31, 2016. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. The U.S. Equity - Small Cap Value composite has been examined for the periods July 1, 2012 - December 31, 2016. The verification and performance examination reports are available upon request.

**Composite Description:** The Small Cap Value Composite consists of accounts that invest in small cap companies that we believe are undervalued by the market.

**Benchmark:** The Russell 2000 Value Index measures the performance of the small cap value segment of the US equity universe. It includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. Index returns are provided for comparison purposes to represent the investment environment existing during the time periods shown. An index is fully invested, includes the reinvestment of dividends and capital gains, but does not include any transaction costs, management fees, or other costs. Holdings of each separately managed account in a composite will differ from the index. An index is unmanaged and an investor may not invest directly in an index.

**Gross of Fees:** Gross of fees performance returns are presented before management fees, but after all trading expenses. Returns are presented net of withholding taxes on dividends, interest income and capital gains where applicable.

**Net of Fees:** Net of fee performance returns are calculated using the maximum stated annual fee of 1.00% applied monthly. Prior to January 1, 2013 net of fee performance was calculated using actual fees. Beginning July 1, 2012, one non-fee paying account was included in the composite. The account represented 100% of the composite assets as of year-end in 2012, 2013, and 2014.

**Performance Calculations:** Results are based on all fully discretionary accounts meeting the composite definition, including those accounts no longer with the firm. Returns are shown in US Dollars, and include the reinvestment of all income. Additional information regarding policies for valuing portfolios, calculating performance, and preparing presentations is available upon request. Past performance is not indicative of future results.

**Composite Dispersion:** The composite dispersion of annual returns is indicated by the performance of individual accounts representing the equal weighted standard deviation of returns. Dispersion of returns is calculated for portfolios included in the composite for the full year.

**3-Year Standard Deviation:** Periods with less than 3 years of data will show "n/a".

**Derivatives, Leverage and Short Positions:** None of these strategies are currently employed by any account in this composite.

**Cash Flow Policy:** As of April 1, 2015 the significant cash flow policy was removed from the composite. Prior to that date, composite policy required the temporary removal of any portfolio incurring a client-initiated significant cash inflow or outflow of at least 10% of portfolio assets. The temporary removal of such an account occurred at the beginning of the month in which the significant cash flow occurred and the account re-entered the composite the first full month of being fully invested.

**Fee Schedule:** 1.00% on first \$10 million; 0.95% on next \$15 million of assets; 0.85% on next \$25 million of assets; and 0.75% on assets exceeding \$50 million. Advisory fees are described on this page and in Form ADV Part 2A. RBC GAM reserves the right to negotiate all advisory fees.

**Minimum Account Size:** There is no minimum account size for this composite.

**Creation Date:** This composite was created on and has an inception date of July 1, 2012.

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