AMG River Road Focused Absolute Value Fund

COMMENTARY

ASSET CLASS | ALL CAP

Class N | ARRFX Class I | AFAVX Class Z | ARRZX

RIVER ROAD ASSET MANAGEMENT®

Average Annual Returns (%)[1] (as of 03/31/21)

	Q1	YTD	1 yr	3 yr	5 yr	Since Incpt.
ARRFX (Class N)	6.63	6.63	51.08	10.87	12.21	11.28[2]
AFAVX (Class I)	6.63	6.63	51.42	11.15	12.47	11.53[3]
ARRZX (Class Z)	6.70	6.70	51.42	11.21	-	9.68[3]
Russell 3000® Value Index	11.89	11.89	58.38	10.99	11.87	10.58[3]

ARRFX (Class N) Expense Ratio (Gross/Net)[4]: 1.15%/1.07%
AFAVX (Class I) Expense Ratio (Gross/Net)[4]: 0.90%/0.82%
ARRZX (Class Z) Expense Ratio (Gross/Net)[4]: 0.86%/0.78%

The performance data shown represents past performance. Past performance is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. The investment return and the principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. For performance information through the most recent month end, please call 800.835.3879 or visit our website at amgfunds.com. From time to time the advisor has waived fees or reimbursed expenses, which may have resulted in higher returns.

The **AMG River Road Focused Absolute Value Fund** (Class N) returned 6.63% for the first quarter of 2021, compared to the 11.89% return for its primary benchmark, the Russell 3000® Value Index. For the 12-month period ending March 31, 2021, the Fund returned 51.08%, versus the 58.38% return for the Index.

Market Overview

A speculative frenzy kicks off 2021

It was a remarkable quarter for stocks, particularly small cap and value, with robust returns capping a historic 12-month recovery. The new year began with a speculative frenzy as investors, particularly retail types, piled into the smallest, cheapest, and lowest quality stocks. At the center of the action was a social media movement targeting stocks with high short interest. The poster child for this bizarre event was GameStop Corp. (GME), which soared from an intra-month low of $17.08 to a high of $483.00. A speculative fever was also evident on the institutional front in the record-shattering activity among SPACs (special purpose acquisition companies). According to Cantor, 91 SPAC IPOs were priced in January alone.

Small cap stocks continued to lead; value posted its best quarter in more than two decades

The explosive rally among small cap and value stocks that started in the wake of the COVID-19 vaccine approval continued through much of Q1. In the first two months of the year, the small cap Russell 2000® outpaced the large cap Russell 1000® by +953 bps and the Russell 3000® Value led its growth peer by +589 bps. In March, Russell's small and mid-cap growth indices took a negative turn, and large cap stocks led as a result. At the same time, value indices continued their steady march higher and are starting 2021 with a solid lead. In fact, this was the largest quarterly outperformance for the Russell 3000® Value versus Growth since the collapse of the internet bubble in 2000. By the end of Q1, the Russell 3000® Value had returned 11.89%, outpacing the Russell 3000® Growth by +1,070 bps.

The strongest 12-month advance since the 1930s

The S&P 500® Index returned 6.17% for Q1, resulting in a 12-month return of 56.35%—the strongest four-quarter advance since the 1930s. The Russell 2000® returned 12.70% for Q1 and a whopping 94.85% for the prior 12 months, the second-best four-quarter advance in the history of the index (since 1979). Over the past two quarters, the Russell 2000® has beaten the Russell 1000® by 27.64%,

[1] Returns for periods less than one year are not annualized.
[2] Since the inception of the Fund's N and I share classes on November 3, 2015.
[3] Since the inception of the Fund's Z share class on September 29, 2017.
[4] Expense ratios effective as of May 1, 2020. The Fund's investment manager has contractually agreed, through at least March 1, 2022, to limit Fund operating expenses. The net expense ratio reflects this limitation, while the gross expense ratio does not. Please refer to the Fund's prospectus for additional information on the Fund's expenses.

which is the biggest spread on record and far above the next closest, which was 19.01% in Q2–Q3 1980.

The Russell 3000® Value returned 58.38% over the prior 12 months, marking the third-strongest 12-month advance in the history of the index (the best since June and July 1983 which returned 61.60% and 63.70%, respectively). While the Russell 3000® Value outpaced its growth peer for the quarter, it still trailed the Russell 3000® Growth return of 64.31% over the prior year.

Although factors shifted in March, high beta and low quality still dominated Q1

According to Style Analytics, the highest beta stocks in the Russell 3000® Value benchmark (top quartile) returned 21.94% for Q1, versus just 3.86% for the lowest (bottom quartile). From a quality perspective, the lowest ROE stocks in the benchmark returned 13.91% versus 9.16% for the highest. Returns for the Russell 3000® Value were also boosted by the 18% of stocks in the index not expected to generate a profit over the next 12 months which, collectively, rose 18.75%. Looking more specifically at March, factor analysis points toward outperformance of higher quality, lower beta stocks in the final month of the quarter, although we generally put little weight in such short periods of analysis.

Performance Review

Based on our analysis utilizing Style Analytics, the Fund's underweight to beta was by far the most significant factor exposure contributing to relative underperformance during the quarter and trailing 12 months. This is unsurprising given the Fund's (and firm's) focus on investing in higher quality companies with sustainable and predictable business models and financial strength, which often leads to lower beta holdings typically associated with Absolute Value® investing.

As a concentrated strategy, we expect the Fund's return profile to be driven by stock selection. However, when factor rotations occur rapidly, they can have a short-term impact on results. The persistence of high beta and low quality leadership within the Russell 3000® Value during Q1 presented a headwind to our style of investing and relative performance.

The most recent period marked the highest rolling 12-month return for the index and the fourth-lowest relative return since the Fund's inception. According to Style Analytics, the highest beta stocks in the index (top quartile) returned a staggering 103.6% compared to the bottom quartile's return of 26.5%. Similarly, the lowest quartile ROE stocks in the index returned 60.4% compared to just 45.7% for the highest ROE stocks.

Confirmation of the low quality rally is evidenced by our conviction system. Using overall conviction as proxy for quality, we saw the lowest conviction stocks in the Fund's universe produce the strongest returns in Q1. The movement from higher risk (lower conviction) to lower risk (higher conviction) yields an almost linear return progression, as seen in the table to the right. Lower conviction stocks (3.5 or lower) within the Fund, which are typically sized smaller on an individual name basis, outperformed the index, while higher conviction stocks (2.0 or above) underperformed. Performance of average conviction holdings (2.5 and 3.0) stocks was mixed.

Over the last several months we have witnessed external market factors and forces contributing to price action, some of which we view as irrational. In the Positioning section, we expand on our management of the risks and opportunities presented in Q1.

For Q1, the key drivers of relative performance included negative stock selection, primarily within financials and communication services, as well as an underweight allocation to energy, the highest returning sector in the index. Positive stock selection within consumer staples and consumer discretionary helped to partially offset this. Lower conviction stocks outperformed while higher conviction stocks underperformed the index. Finally, the underperformance of large cap and smaller cap stocks detracted, while mid cap stocks in the Fund modestly outperformed.

What worked...

The sector with the highest contribution to Fund return in Q1 was consumer discretionary. The largest positive contributing holding during the quarter was BJ's Wholesale Club Holdings Inc. (BJ, +21%), a warehouse club retailer with more than 200 stores primarily located in the eastern United States. During the period, BJ released Q4 results in line with high expectations, capping an extraordinary year. During the quarter, same-store sales increased 15.9% excluding fuel prices, benefiting from higher traffic and increased average ticket size. Higher gross profit, improved retail execution, and strong expense controls more than offset COVID-19-related costs, driving earnings before interest, taxes, depreciation, and amortization (EBITDA) growth of 37% with EBITDA margins of 5.0%, up +90 bps compared to the prior year quarter. New membership growth continued in Q4, powering an 11.3% increase in the total member base year over year. New members continue to skew younger with more digital engagement, higher premium product mix, and above-average spending. This should support future merchandise sales growth beyond the pandemic. Despite the stock's strong performance over the past year, we believe the market still underestimates the long-term value created by BJ's expanded and more profitable membership base. Additionally, we believe there remains substantial room to improve store metrics and profitability through execution of strategic objectives and expanding product and service offerings. Finally, we see further upside from store growth as BJ looks to expand its footprint in new and existing markets, supported by the recent surge in cash flow. We opportunistically trimmed the position in BJ during the quarter when the stock traded sharply higher for what we believed to be non-fundamental reasons, though we maintain a position and remain positive on the shares.

Another top contributor during the period was Berkshire Hathaway Inc. (BRK.B, +10%), a conglomerate with a diverse group of wholly owned operating companies and other public/private investments. Berkshire's overall book value per share grew 8.6% in the quarter and 9.8% year over year driven by further appreciation of the equity portfolio, internal cash generation, and share buybacks. Share repurchases were $8.8 billion in Q4, bringing the full year total to $24.7 billion at an average price representing 1.15x year-end book value. After reducing the share count -5% in 2020 (-1.7% in Q4 alone), buybacks continued into 2021, reducing the share count an additional -0.8% by mid-February. Results within insurance were particularly strong, highlighted by pre-tax earnings of $1.08 billion, up 88% year over year against a weak comparison, though still up 17% sequentially.

In the annual letter to shareholders, Chairman and CEO Warren Buffett highlighted Berkshire's largest equity investment, its 5.4% stake in Apple Inc. (AAPL), which was worth $120 billion at the end of the year and now represents Berkshire's third most valuable asset, behind the insurance business and just slightly less than Burlington Northern Santa Fe Corp. (BNSF). This investment, which carries a cost basis of just ~$36 billion, has been one of the most successful in Berkshire's history. This is important to recognize given frequent criticism of Buffett's recent investment performance. As we have noted previously, the AAPL investment, when combined with the $138 billion of cash on the balance sheet, represented close to 50% of Berkshire's total market capitalization at the end of 2020. We believe this highlights the market's undervaluation of Berkshire's operating businesses. As such, we opportunistically added to the position during the quarter as it remains one of the most attractive combinations of risk-to-reward in the Strategy's opportunity set.

Another positive contributor was LKQ Corp. (LKQ, +20%), a global distributor of aftermarket and recycled replacement parts for vehicle repair. LKQ reported another solid earnings report, demonstrating management's skill in navigating a difficult COVID-19-impacted operating environment. While total revenues declined, a laser focus on controllable costs drove exceptionally strong margins, including a new record for the North America segment. Free cash flow was also impressive, posting a record $1.2 billion in 2020, owing to skillful working capital management. Net debt/EBITDA is now below 2x—down from 3.5x in 2018 and at the lowest level since 2015—earning credit rating upgrades from both Moody's and S&P during the quarter. We trimmed the position early in the quarter as the price approached assessed value but added to the position soon thereafter as volatility provided a brief opportunity to buy the stock at compelling prices.

What didn't work…

The sector with the lowest contribution to Fund return was utilities (+7 bps) driven by bottom contributor, Vistra Corp. (VST, -19%), partially offset by outperformance of AES Corp. (AES, +15%).

The largest negative contributor during the quarter was Vistra Corp. (VST, -19%), an independent producer and retailer of electricity. FAV initiated a position roughly a week before the historic winter storm Uri hit Vistra's largest market, Texas. The Texas market is unique as its electricity market is "deregulated" meaning electricity prices are market based and a single utility does not have a monopoly on electricity generation/distribution in a given area. Historically, VST has benefited from volatility in power prices given its conservative hedging policy, ownership of generation and retail electricity assets, and reliable fleet. As the initial reports of rolling blackouts came in, it appeared Vistra's electricity generation was holding up relatively well and that VST would benefit from electricity prices that hit the price cap. However, as natural gas pipelines began to freeze many of VST's suppliers claimed force majeure and failed to honor contracts or were unable to perform delivery commitments. Management was unable to secure enough fuel to keep its generation plants operating while its retail customers were less impacted by blackouts than other consumers elsewhere in the state, resulting in a collapse of the firm's natural hedge position. VST management decided to keep the power on for its customers during the storm, which required it to buy natural gas on the spot market at significantly higher prices. Although this was the correct decision for its customers, when combined with a systematic breakdown in ERCOT's (Electric Reliability Council of Texas) pricing mechanisms, the events surrounding winter storm Uri led to an estimated $900 million to $1.3 billion loss in the period. There is a chance the company can recoup some of the pricing-related losses, but the timing of any recovery is uncertain. VST is in the early innings of a multi-year portfolio transition as it adds renewable energy and reduces its coal exposure (which should lead to multiple expansion), while simultaneously returning a significant amount of capital to shareholders through share repurchases, dividend growth, and debt reduction. While the timing is unfortunate and the unexpected one-time reduction in free cash flow delays the return of capital roughly one year, we believe VST's management decisions will ultimately benefit returns over the long term. As many retail competitors declared bankruptcy, VST will likely continue growing share in the Texas market and has surely garnered favor with regulators as a good actor in this unfortunate event.

Another bottom contributor during the quarter was Liberty Broadband Corp. (LBRDK, -5%), a holding company with a 26% ownership stake in Charter

Communications Inc. (CHTR). Disappointment stemmed from CHTR adding fewer internet subscribers in Q4 than consensus expectations. However, internet add-ins were very strong the first three quarters of 2020, and CHTR's free 60-day offer for COVID-19-impacted individuals pulled growth forward. A portion of promotional subscribers transitioned to paying subscribers and contributed to the revenue and EBITDA beat for the quarter. Additionally, during the quarter it was announced that LBRDK bumped up against its 26% CHTR ownership cap which means LBRDK will participate in future CHTR buybacks such that LBRDK's ownership remains at or below 26%. This should generate roughly $1.9 billion in after-tax proceeds in 2021 that can be channeled into LBRDK buybacks. During the quarter, repurchasing a share of LBRDK was equivalent to purchasing CHTR at an 18.5% discount to the market price. We maintained the position.

Also among the negative contributors was global consumer packaged goods company Unilever PLC Sponsored ADR (UL, -6%). The stock lagged following underwhelming 2H earnings driven by higher-than-expected COVID-19-related costs and marketing expenses. Organic growth was strong at 3.5% as demand remained high for UL's antibacterial and germ-killing products, and its retail foods business benefited from more in-home eating occasions. Despite modestly lower margins in 2020, UL's cash conversion was strong with free cash flow of €7.7 billion, up €1.5 billion over 2019. Further, the company increased the dividend by 4% and completed the unification of its legal structure, which should improve the company's ability to divest non-core brands, including its tea business. We continue to view UL as well positioned over the longer term given its emerging market exposure, improving portfolio mix, consistent organic growth, strong market share, and attractive returns on invested capital. We continued to build the position during the quarter.

Positioning

Investment activity in Q1 was high with the majority of activity occurring in the first two months of the year. Q1 activity included five new positions established and two eliminated. Of the positions sold, both were due to valuation. As of March 31, the Fund held 23 positions compared to 20 held at the end of Q4.

Trading activity peaked toward the end of January and early February as the team responded to market volatility related to the meteoric rise in heavily shorted stocks. As short sellers moved to cover positions, we saw sharply rising prices for many stocks with even moderate short interest and, more selectively, falling prices for some high quality businesses (perhaps through forced liquidation to cover short bets). The FAV team took advantage of this fleeting opportunity to lock in gains for several positions, including Discovery Inc. (DISCK), Hostess Brands Inc. (TWNK), BJ's Wholesale Club Holdings Inc. (BJ), and Avaya Holdings Corp. (AVYA), all of which had relatively high short interest. Over a two-week period, nine positions were trimmed or exited, and proceeds were deployed into 10 different positions, including three new holdings. As the team moved to capitalize on these market movements, portfolio activity, as measured by turnover, reached 18% by the end of February (for comparison, activity in 2020 was 78%).

The largest change in sector exposure was a 7% bps increase to consumer staples driven by the addition of two new holdings, Molson Coors Beverage Co. (TAP), discussed below as the largest new holding, and Fomento Economic Mexicano SAB de CV Sponsored ADR (FMX), as well as continuing to build the position in Unilever PLC Sponsored ADR (UL). This was partially offset by trimming BJ and TWNK, which traded near assessed value during the GME frenzy. FMX is a holding company with equity stakes in Coca-Cola FEMSA (KOF-US), the largest Coca-Cola bottler in the world, Heineken NV (HEIA-NV), the largest European brewer, and its wholly owned operating businesses. The largest of these operating businesses include a chain of 19,600 Oxxo branded convenience stores and 3,300 pharmacy locations. FAV III initiated FMX when the operating businesses were trading at 7x EBITDA, a significant discount to the historical multiple of 14x, after marking-to-market its equity stakes in Heineken and Coca-Cola FEMSA. While the multiple compression was supported by the negative impact pandemic restrictions had on its Oxxo stores with traffic declines outpacing ticket growth, FMX has low leverage of <1x and consistent free cash flow generation providing protection from further downside. On the upside, as Mexico's economy reopens, the River Road team anticipates Oxxo's same-store sales (SSS) will recover to prior trends (average SSS were 6.1% from FY 2015–FY 2019) and new store growth will return to its >4% historical rate. Lastly, we believe Oxxo's digital banking initiatives—including a voucher system that provides Mexico's large unbanked population (~60% of the population) a vital connection to the digital economy by paying in-store with cash for online subscriptions such as Netflix—will continue to strengthen FMX's relationships with consumers.

New purchase...

The largest new position added during the quarter was Molson Coors Beverage Co. (TAP). Molson Coors Brewing is the world's fifth-largest brewer with a portfolio of popular brands including Coors Light and Molson Canadian in Canada, Coors Light, Miller Lite, Blue Moon, Leinenkugel, and Vizzy in the United States, and Carling in the United Kingdom. The company brews, markets, and distributes beer in the United States (73% of FY 2020 revs.), Europe (15%), and Canada (12%). TAP's Molson and Coors were founded in 1786 and 1873, respectively. TAP is based in Chicago. Gavin Hattersley (56) succeeded Mark Hunter as CEO in September 2019 after serving as the head of the MillerCoors JV since 2015.

TAP has strong market share positions including 22% market share in North America (#2 brewer) and 18% market share in Europe. The modern brewery industry remains concentrated in the U.S. with TAP and Anheuser-Busch (BUD) controlling 63% of the market, resulting from several competitive advantages: First, brewers benefit from scale as it creates cost advantages versus smaller peers through lower input costs and the ability to leverage fixed costs over higher volumes. Second, product distribution presents barriers to entry. The three-tier distribution framework in the U.S. requires that brewers sell to distributors before retailers which creates the opportunity for TAP and BUD to incentivize distributors to maintain market position, while also allowing TAP to maintain a distribution advantage given its second-largest network of 400 independent distributors. Lastly, brands are important and TAP's customers are among the most loyal with the Miller Lite and Coors Light brands consistently ranking in the top five U.S. beer brands.

These competitive advantages drive TAP's predictable and sustainable results including consistent free cash flow generation across the economic cycle, supporting its leverage ratio of 3.5x net debt/EBITDA. Significant liquidity from cash on the balance sheet and access to credit facilities further limits the downside typically associated with a higher leverage profile. Additionally, free cash flow generation, along with peer transactions at similar or higher multiples, is supportive of the 9.9x EBITDA multiple River Road uses to value TAP.

TAP's EBITDA multiple has historically traded at a discount to peers as its organic growth rate has trailed the industry as consumer preference has shifted toward more premium beers and other alcoholic beverages. TAP has been slow to respond to changes in consumer taste; however, we are optimistic management's "Beyond Beer" revitalization strategy will help close the valuation gap. The "Beyond Beer" expansion was originally discussed at the beginning of Gavin Hattersley's tenure as CEO in Q4 2019. Management successfully executed this initiative during the pandemic, resulting in a more diverse product portfolio in higher growth categories. For example, management believes TAP can achieve 10% market share in the hard seltzer category by year-end 2021. Further, new partnerships include joint ventures with premium-branded Yuengling, to expand distribution beyond the eastern U.S. and Coco-Cola Co. (KOF) to brew a Topo-Chico Hard Seltzer. We believe these new products coupled with revitalized core portfolio brands will reaccelerate top-line growth, while corporate headquarters and brewery footprint restructurings will drive higher margins moving forward, both of which should lead to multiple expansion.

The most significant near-term risk to this investment is an extended continuation of pandemic related on-premise restrictions (e.g., restaurants, bars, sport venues), which would continue to be a headwind to sales and profit margins given TAP's significant fixed cost structure, especially in Europe where 55% of FY 2019 sales were on-premise. However, in the United States, demand for TAP's products in the off-premise channel, especially key brands such as Miller Lite and Coors Light, offset weakness in the on-premise channel resulting in revenue growth in Q4 2020. Additionally, the U.S. and the U.K. are ahead of the curve relative to the global COVID-19 vaccine rollout, which should result in the reopening of these economies in the near term.

Using a 9.9x multiple on TAP's FY 2021e EBITDA less net debt and non-controlling interests, we arrived at an assessed value of $64 per share and an overall conviction of 3.5 (1=highest, 5=lowest). At the time of initial purchase, TAP traded at a -30% discount to our assessed value. The company is followed by River Road Equity Research Analyst Allen F. Harris.

Outlook

River Road's market outlook is driven by five key factors: 1) valuations/earnings; 2) monetary policy/credit trends; 3) fiscal policy/Washington; 4) CEO/investor sentiment; and 5) a few "wildcard" factors we believe may impact equity returns in the year ahead. While we do not view the firm's outlook as a market prediction per se, our view on the economic and market environment can have an impact on stock valuations, conviction assessments, and overall portfolio positioning.

Valuations remain high...

Despite rising earnings expectations during the first quarter, the Russell 3000® now trades at 23.5x forward earnings expectations, essentially unchanged since the beginning of year, according to FactSet. The Russell 3000® Value trades at 18.9x, up slightly from 18.0x. Of course, these measures are well above their respective long-term averages of 16.5x and 14.3x.

River Road's proprietary valuation metric is the weighted average discount to assessed value for the Fund's holdings. As of March 31, the discount to assessed value for the Fund was 79.7%. While certainly elevated this is a significant improvement from the 83.3% reading at the end of 2020. However, the underlying multiple supporting valuations has reached a new high of 11.2x, a worrisome observation. We do not interpret this figure to imply impending doom, but we do view it as an indicator of low opportunity in our investment universe. Notably, the Fund universe discount to assessed value stood at 87.4% at the end of March compared to 86.8% at the end of 2020. The Fund was able to increase the relative valuation gap by opportunistic trading activity during the height of the GME frenzy. Most importantly, activity during the quarter resulted in a more attractive risk-to-reward for the Fund with both the discount in the Fund and weighting in higher conviction stocks improving. As of March 31, the Fund's weighting in higher conviction stocks increased to 60.3%, an increase of +262 bps over Q4 and nearly 2x the weighting in the Fund universe.

Fund remains overweight small cap

Within the Fund universe, discounts among smaller cap stocks dramatically declined over the last four months, driven by sharply rising prices, particularly among stocks with average or below-average conviction. While small cap stocks remain attractive relative to large cap externally, the number of small cap stocks within our opportunity set trading below 80% of assessed value declined during the quarter. FAV III remains overweight smaller cap stocks (<$5 billion in market cap) with 12% exposure versus just 8% within the Russell 3000® Value Index. We found one attractively priced smaller cap company to introduce during Q1, GoHealth Inc. (Cl A) (GOCO), and we continue to assess the opportunities for attractively priced higher quality small cap stocks.

Fed stays the course

There is little to report on the monetary front as the U.S. Federal Reserve (the Fed) continues to indicate it will remain highly accommodative through at least 2021. We see inflationary pressures building in the manufacturing and commodity sectors and continue to believe a hotter-than-expected inflation reading may spook Wall Street in 2021, especially given the valuation backdrop. From a portfolio perspective, this has encouraged us to focus on companies with strong pricing power. However, the factors historically associated with secular inflation that would truly spook the Fed, such as severe labor, materials, or capacity constraints, do not appear to be on the horizon. According to BofA Global Research, rising inflation is also not necessarily negative for multiples if the CPI remains below 4%, with most economists expecting about 3% in 2021. However, a sharp rise in wages would be negative for small caps, as they are 2x more labor intensive compared to large caps.

President Biden appears to have borrowed Ben Bernanke's helicopter

Fiscal stimulus combined with monetary stimulus can be a powerful driver of economic and earnings growth, which is why both are included in our outlook model. President Biden understands this and is pulling out all the stops, delivering a third round of direct stimulus payments and promising $3-$4 trillion in spending measures focused on infrastructure, climate change, education, and inequality. Of course, regardless of what you might read on a trending "Modern Monetary Theory" website, these programs ultimately come at a cost. Thus, we expect to see higher individual and corporate taxes in 2022. Biden's proposed tax increases would reduce S&P 500 EPS by approximately -7%, with information technology, consumer discretionary, and health care hit hardest. If this occurs, especially as earnings momentum is slowing, inflationary pressures are building, and the Fed is poised to taper, it would likely exert significant downward pressure on what are currently extremely high multiples. Furthermore, according to BofA, every +100 bps rise in debt cost translates to a 2% hit to EPS. We suspect investors will begin to focus more keenly on these risks in the second half of 2021.

Economies are re-opening, housing remains red hot, and M&A is on the rise

All our wildcard factors remain strongly positive. Over the past few months, vaccine distribution has improved significantly. Thus, although a "fourth wave" of the virus is emerging due to new variants, we expect state and regional economies will continue to steadily re-open in the coming months. Another positive is the red-hot housing market, which is closely connected to the performance of small caps and is well positioned for a multi-year run as interest rates and inventories remain extremely low, employment improves, and younger workers seek a place to live AND work.

Finally, corporate spending is on the rise as the record amounts of cash held by companies is being spent on capex, dividends, buybacks, AND M&A. Capex and M&A are especially positive for small caps. While M&A is typically a late cycle phenomenon, in this compressed "Benjamin Button" cycle, we appear to be experiencing a peak-cycle boom in M&A, including several transactions positively impacting portfolio holdings. There are also numerous reasons to expect heightened capex over the next few years, including a sharp rise in infrastructure spending, underinvestment in recent years, and increased capacity utilization.

The market shows few, if any, signs of retreating in the near term; time to worry?

While absolute valuations appear to be alarmingly high, relative valuations and other cyclical factors (strong housing, low interest rates/tight credit spreads, broad earnings growth, elevated M&A) remain highly supportive for value. Additionally, we believe record monetary and fiscal stimulus will continue to provide rocket fuel for the recovery as economies re-open. Perhaps the biggest concern to the near-term narrative is that every dark cloud looming over this recovery has suddenly vanished. As every seasoned investor knows, extreme optimism (as evidenced by high margin debt, the red-hot IPO/SPAC market, strong consumer/investor confidence, etc.) is the enemy of bull markets.

Transition to mid-stage should support relative performance

Despite the challenging relative performance in Q1, we continue to strongly believe the Fund is well positioned for what lies ahead. As we move out of the early phase of the recovery, there is evidence the "high beta, low quality" stage is fading, with the market transitioning to a more supportive, mid-stage recovery in March. Analysts at BofA Global Research agree, with their long-standing market cycle model moving into the mid-stage around late February. If this is the case, relative performance should continue to improve in the months ahead.

Fortunately, we believe the Fund is well positioned for the uncertainty of 2021 and reflects an attractive balance of value, quality, and growth. According to FactSet, the Fund's valuation (as measured by EV/EBITDA) is just 10.5x versus 13.8x for the Russell 3000® Value benchmark. Quality, as measured by five-year average return on equity (ROE), is 14.5% versus 14.1% for the benchmark. Finally, the Fund's expected long-term growth (as measured by published long-term estimates) is a healthy 9.2% versus 10.3% for the benchmark.

The views expressed represent the opinions of River Road Asset Management LLC, as of March 31, 2021, are not intended as a forecast or guarantee of future results, and are subject to change without notice.

Top Ten Holdings (%)[5] (as of 03/31/21)

Holding	% of Net Assets
Berkshire Hathaway Inc, Class B	9.64
Liberty Broadband Corp, Class C	9.16
Fidelity National Financial Inc	5.98
Comcast Corp, Class A	5.80
Liberty Media Corp-Liberty SiriusXM, Class C	5.79
LKQ Corp	5.22
Cisco Systems Inc	4.93
Bristol-Myers Squibb Co	4.77
Unilever PLC ADR	4.61
Molson Coors Beverage Co, Class B	4.39
TOTAL %	60.29

[5] Mention of a specific security should not be considered a recommendation to buy or a solicitation to sell that security. Holdings are subject to change.

Disclosure

Investors should carefully consider the fund's investment objectives, risks, charges, and expenses before investing. For this and other information, please call 800.835.3879 or download a free prospectus. Read it carefully before investing or sending money.

Past performance is no guarantee of future results.

The Fund is subject to risks associated with investments in small-capitalization companies, such as erratic earnings patterns, competitive conditions, limited earnings history, and a reliance on one or a limited number of products.

The Fund is subject to risks associated with investments in mid-capitalization companies such as greater price volatility, lower trading volume, and less liquidity than the stocks of larger, more established companies.

The Fund is subject to the risks associated with investments in emerging markets, such as erratic earnings patterns, economic and political instability, changing exchange controls, limitations on repatriation of foreign capital, and changes in local governmental attitudes toward private investment, possibly leading to nationalization or confiscation of investor assets.

Investing in PTPs (including master limited partnerships) involves risks in addition to those typically associated with publicly traded companies. PTPs are exposed to the risks of their underlying assets, which in many cases includes the same types of risks as energy and natural resources companies. PTPs are also subject to capital markets risk. PTPs may lose their partnership status for tax purposes. The status as a regulated investment company may be jeopardized if it does not appropriately limit such investments in PTPs or if such investments are recharacterized for tax purposes.

Active and frequent trading of a fund may result in higher transaction costs and increased tax liability.

A greater percentage of the Fund's holdings may be focused in a smaller number of securities, which may place the Fund at greater risk than a more diversified fund.

Investments in international securities are subject to certain risks of overseas investing including currency fluctuations and changes in political and economic conditions, which could result in significant market fluctuations. These risks are magnified in emerging markets.

The Fund is subject to special risk considerations similar to those associated with the direct ownership of real estate. Real estate valuations may be subject to factors such as changing general and local economic, financial, competitive, and environmental conditions.

Companies that are in similar businesses may be similarly affected by particular economic or market events; to the extent the Fund has substantial holdings within a particular sector, the risks associated with that sector increase.

Market prices of investments held by the Fund may fall rapidly or unpredictably due to a variety of economic or political factors, market conditions, disasters or public health issues, or in response to events that affect particular industries or companies.

The Fund invests in value stocks, which may perform differently from the market as a whole and may be undervalued by the market for a long period of time.

The S&P 500® Index is a capitalization-weighted index of 500 stocks. The S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Unlike the Fund, the Index is unmanaged, is not available for investment, and does not incur expenses.

The Russell 1000® Index is a market capitalization-weighted index, meaning that the largest companies constitute the largest percentages in the index and will affect performance more than the smallest index members.

The Russell 2000® Index is a small-cap stock market index of the bottom 2,000 stocks in the Russell 3000® Index. The Russell 2000® Index is considered the most common benchmark for mutual funds that identify themselves as "small-cap."

The Russell 3000® Index is composed of the 3,000 largest U.S. companies as measured by market capitalization, and represents about 98% of the U.S. stock market.

The Russell 3000® Growth Index measures the performance of the broad value segment of the U.S. equity universe. It includes those Russell 3000® companies with higher price-to-book ratios and higher forecasted growth values.

The Russell 3000® Value Index measures the performance of the broad value segment of the U.S. equity universe. It includes those Russell 3000® companies with lower price-to-book ratios and lower forecasted growth values. The Index reflects no deduction of fees, expenses, or taxes.

Unlike the Fund, the Indices are unmanaged, are not available for investment, and do not incur expenses.

Any sectors, industries, or securities discussed should not be perceived as investment recommendations. Any securities discussed may no longer be held in the Fund's portfolio. It should not be assumed that any of the securities transactions discussed were or will prove to be profitable, or that the investment recommendations we make in the future will be profitable.

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