WASATCH GLOBAL INVESTORS

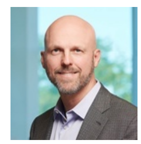
Quarterly Commentary

Wasatch Small Cap Value Strategy

DECEMBER 31, 2019

Stock Selection Fueled a Strong Year for the Strategy

PORTFOLIO MANAGER



Jim Larkins
Lead Portfolio Manager
20 YEARS ON STRATEGY / 23 YEARS AT WASATCH

OVERVIEW

Small-cap value stocks moved steadily higher in the fourth quarter, closing out a positive year for both the category and the U.S. equity market as a whole. The combination of improving global growth, accommodative U.S. Federal Reserve policy, and signs of progress on the U.S.-China trade dispute helped equities build on their earlier gains. The Russell 2000® Value Index, the strategy's benchmark, rose 8.49% in the quarter and 22.39% for the full year.

The strategy posted a robust absolute return and outpaced the benchmark in 2019. We generated the best relative performance in the first half of the year thanks to our effective individual stock selection. Our results moderated in the third quarter, but the strategy nonetheless retained the majority of its earlier return advantage in a time of elevated market volatility. The fourth quarter proved to be somewhat more challenging, however, as we fell short of the benchmark amid strength in higher-risk stocks. Still, we are gratified that our stock-selection process enabled the strategy to outperform in a year that featured unusually high returns for the broader market and frequent rotations among sectors and investment styles. While our relative performance can shift from quarter to quarter, we think our focus on best-in-breed, undervalued companies was a key factor not just in the strategy's outperformance in 2019, but also over the three-year, five-year, 10-year and since-inception periods.

DETAILS OF THE QUARTER

The strategy's underperformance in the information-technology sector accounted for most of the fourth-quarter shortfall against the benchmark. Although the majority of the strategy's holdings in the sector registered a gain, they did not keep pace with the types of higher-risk stocks that drove the Index's recent returns. In addition, shares of Ebix, Inc. (EBIX) lagged by a wide margin due to investors' uncertainty regarding the company's plan to spin out its India operations in an initial public offering. While we are maintaining the investment on the belief that the stock continues to represent a long-run growth opportunity, we are doing so with a below-average position size to account for the potential risks. On the plus side, the tech sector was home to two of the strategy's most notable contributors. Fabrinet (FN), a contract manufacturer of optical components that we have held since early 2011, delivered a sizable stock-price gain due to strength in its core business and emerging growth opportunities in the industrial space. Tower Semiconductor, Ltd. (TSEM) was another notable winner in technology. The stock performed poorly in 2018 as Tower management renegotiated contracts with some key customers, but our analysis showed that the business remained firmly on track. We therefore added to our position early in 2019, and the strategy benefited as the company's improving results began to feed through to its stock price over the course of the year.

Outside of Ebix, two other holdings stood out as detractors. Shares of the sectional furniture maker Lovesac Co. (LOVE) weakened due to the impact of higher tariffs and the adverse effect that its investments in future growth had on its 2019 profits. Believing both of these short-term issues have obscured the company's healthy brand and improving growth prospects, we chose to maintain the position. LGI Homes, Inc. (LGIH) also finished as a key detractor, as the stock pulled back after strong a strong move in the third quarter. We continue to like LGI's long run fundamentals, and we maintained the position.

The industrials sector continued to be an important driver of positive performance in the final three months of the year. We continued to find the sector home to a number of attractive businesses that we believe are underappreciated by Wall Street. Industrials was our strongest-contributing sector relative to the benchmark for the three- and 12-month periods. Kadant, Inc. (KAI), a supplier of equipment and components used in paper production, paper recycling, recycling and wood processing, was the top contributor for the quarter. The company generates a large percentage of its revenues from replacement parts and consumables, resulting in robust and stable cash flows. Altra Industrial Motion Corp. (AIMC) rebounded from weak third-quarter performance as accelerating economic growth appeared to make investors more comfortable with the company's recent acquisitions. While we like the business, we are not at a full weight due to the company's high debt levels. Regional airline Allegiant Travel Co. (ALGT) was another key contributor in industrials. The stock lagged in 2018 as the airline transitioned to a new fleet, but earnings rebounded in 2019 as this expenditure was completed.

OUTLOOK AND POSITIONING

Our approach focuses on stock selection and avoids making "calls" on the economy, specific sectors, or the market as a whole. We are therefore maintaining a steady methodology that emphasizes individual company research rather than attempting to make broad predictions about the year ahead. At the same time, we also recognize that the market could be vulnerable to adverse surprises after such a positive year—particularly as the November 2020 elections draw closer.

Accordingly, we are maintaining a tilt toward what we consider higher-quality, fundamentally sound, and financially healthy companies. While our focus on quality and value was somewhat of a headwind in the most recent quarter, we think it is appropriate for a time in which investors may not be able to count on a continued rally in the broader market to support returns. We are therefore striving to maintain a balanced, "all-season" portfolio that we believe can perform well across a wide range of scenarios.

We are also actively looking for fresh ideas among "Fallen Angels"—our term for growth companies whose stocks have hit what we believe is a short-term bump in the road. With value opportunities having grown increasingly scarce in the rising market, we think these types of companies—as distinct from more traditional value investments—could be an important source of return in 2020.

As always, our focus is on maintaining a deep understanding of the inner workings of the individual companies we hold in the portfolio. We believe this disciplined approach—highlighted by our focus on companies with solid balance sheets and/or durable business models—can help the strategy build on its outperformance of 2019.

Thank you for the opportunity to manage your assets.

Sincerely,

Jim Larkins

The Russell 2000 Value Index measures the performance of Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. The Russell 2000 Index is an unmanaged total return index of the smallest 2,000 companies in the Russell 3000 Index, as ranked by total market capitalization. The Russell 3000 Index is an unmanaged total return index of the largest 3,000 U.S. companies based on total market capitalization. The Russell 2000 Index is widely used in the industry to measure the performance of small company stocks.

You cannot invest directly in these or any indexes.

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An initial public offering (IPO) is a company's first sale of stock to the public.

This commentary is intended to provide you with information about factors affecting the performance of the Wasatch Small Cap Value strategy during the period. References to individual companies should not be construed as recommendations to buy or sell shares in those companies. Wasatch analysts closely monitor the companies held in the Small Cap Value strategy. If a company's underlying fundamentals or valuation measures change, Wasatch will reevaluate its position and may sell part or all of its holdings.

Past performance is not indicative of future results.