



Investor / Institutional  
WMCVX / WICVX

# Wasatch Small Cap Value Fund

JUNE 30, 2023

## Our Balanced Approach Led To Strong Outperformance

### OVERVIEW

Small-cap value stocks registered gains in the second quarter, as measured by the 3.18% return of the Russell 2000® Value Index. The Index finished June in positive territory on a year-to-date basis with a gain of 2.50%.

The Wasatch Small Cap Value Fund—Investor Class was up 7.04% in the second quarter and outpaced the Index in the first six months of the year with a total return of 13.01%. We believe this strong showing is a function of not only our focus on higher-quality companies but also our emphasis on seeking balance through holdings in “growthier” segments of the small-cap universe in addition to the traditional value universe. Small-cap growth stocks outperformed the broader small-cap market by a wide margin in the quarter thanks to the backdrop of falling inflation and expectations that the U.S. Federal Reserve would soon pause its long series of interest-rate increases. The Fund was well-positioned for these circumstances, contributing to positive performance versus the Index.

### DETAILS OF THE QUARTER

The Fund’s growth tilt is achieved, in large part, through its holdings in “Fallen Angels”—our term for growth companies that have hit a bump in the road and whose stocks have dropped into value territory. Working closely with fellow team members who manage Wasatch’s growth

### FUND MANAGERS



**Jim Larkins**  
Lead Portfolio Manager

24 / 27  
YEARS ON FUND / YEARS AT WASATCH



**Austin Bone**  
Portfolio Manager

3 / 7  
YEARS ON FUND / YEARS AT WASATCH

*Data show past performance, which is not indicative of future performance. Current performance may be lower or higher than the data quoted. For the most recent month-end performance data, visit [wasatchglobal.com](http://wasatchglobal.com). Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. The Advisor may absorb certain expenses, without which total returns would have been lower. Wasatch Funds will deduct a 2% redemption fee on Fund shares held 60 days or less. Performance data do not reflect this redemption fee or taxes. **Total Expense Ratio: Investor Class—1.16%, Institutional Class—Gross: 1.06%, Net: 1.05%. The Advisor has contractually agreed to limit certain expenses to 1.50% for the Investor Class and 1.05% for the Institutional Class through at least 1/31/2024.***



portfolios, we can quickly access the research Wasatch has already gathered on Fallen Angels and determine if an investment makes sense for the Small Cap Value Fund. We were somewhat below our typical weight in Fallen Angel companies in 2022, and we worked to increase their representation in the portfolio as we found attractive opportunities.

As market conditions have normalized, many of our Fallen Angels have rebounded and made strong contributions to performance. One such stock is **Saia, Inc. (SAIA)**, a trucking company we added to the portfolio in the third quarter of 2022. At the time, we thought Saia's shares had been oversold in the first half of 2022 on concerns about the effects of rising inflation and slowing economic growth. While the industry has indeed seen some pressure in terms of tonnage, Saia has executed well by maintaining pricing discipline rather than by cutting prices to gain volume and the stock has bounced back. Shares of **Trex Co., Inc. (TREX)**, a maker of composite decking materials, also recovered amid the improving outlook for the home-improvement business. Both Saia and Trex were among our top contributors in the second quarter. We believe holdings such as these underscore the merits of our Fallen Angel strategy as a way to unearth opportunities other value managers may miss.

The financials sector was an area of strength for the Fund in the second quarter. Financials came under broad-based pressure in March after the failure of several banks, but our analysis showed that the Fund's holdings in the sector weren't experiencing similar difficulties and remained fundamentally sound. Our banks have a solid base of deposits and generally feature strong franchises, either from the deposit side or from favorable geographic profiles. We believe these traits have helped their performance considerably as the stocks of healthy banks began to recover in the past three months. We further benefited from positions in non-bank financials that performed well, including asset manager **Artisan Partners Asset Management, Inc. (APAM)** and investment banking firm **Moelis & Co. (MC)**.

**UFP Technologies, Inc. (UFPT)**, a manufacturing outsourcing company for the health-care, industrials, and consumer-facing sectors, was the leading contributor to Fund performance. We bought the stock near the end of 2022 as an "Undiscovered Gem," our name for inexpensive, growing companies that are flying below Wall Street's radar. Investors have since begun to take notice of the company's ability to capitalize on the secular growth of the broader medical market, including robotic surgery. UFP has also benefited from an improving business mix following its expansion into new markets. The company raised its outlook at an investor meeting in June, adding further fuel to the stock's rally.

On the negative side, manufactured housing producer **Skyline Champion Corp. (SKY)** was the largest detractor from Fund performance for the quarter. The stock had been performing well year-to-date until it sold off in June after an earnings report that disappointed investors. We maintained the position, as we think the company is poised to capitalize on the need for more entry-level housing in the United States over the next five to 10 years.

**ServisFirst Bancshares, Inc. (SFBS)** also underperformed due to lingering investor concerns about regional banks. We continue to have a favorable long-term view of ServisFirst's ability to drive profitable growth, given our positive take on the company's management team and exposure to fast-growing areas in the southeastern United States.

**Fox Factory Holding Corp. (FOXF)**, a producer of engineered components for bicycles and various power-sports vehicles, also lagged this quarter due to cyclical concerns regarding the bicycle end market following strong demand in recent years. We continue to view Fox as a long-term holding. We see positive indicators that the company can continue to take market share and benefit from secular growth drivers at the industry level, such as electric bicycles.

Our position in **National Storage Affiliates Trust (NSA)** detracted as well. High mortgage rates have led to fewer people moving, which in turn has depressed demand for storage. We think the stock has been overly punished, and



we're encouraged by the combination of insider buying, share buybacks and fundamentals that appear set to bottom. (*Current and future holdings are subject to risk and change.*)

## OUTLOOK

Artificial intelligence (AI) was one of the most-discussed developments in the quarter as investors sought to find companies most likely to be winners in this new and growing area. As is the case with most topics, we don't look at AI from a top-down perspective. Instead, we're considering how it's affecting each of our individual companies. In many cases, management teams see AI technology as a meaningful driver of their businesses in the coming years. Three portfolio companies in particular stand out as potential beneficiaries. **Fabrinet (FN)**, an outsource manufacturer of optical equipment, is positioned to capitalize on the trend since its end markets include data-center providers—an industry that could see new business incrementally created by AI. Semiconductor capital equipment suppliers **Nova Ltd. (NVMI)** and **Veeco Instruments, Inc. (VECO)**, which are "pick and shovel" plays that can benefit from the need for increased computing, also appear to be well-positioned for the growth of AI. More broadly speaking, we're optimistic that increasing adoption of AI will accelerate the shift to the cloud and create a wide range of stock-specific opportunities in the years ahead.

In terms of our portfolio activity, turnover among the Fund's holdings slowed down somewhat compared to its level of a year ago. We think this is a signal of an improved market environment. We view our small-cap value strategy in terms of "competition for capital"—we only add new names to the Fund if we believe they offer more compelling opportunities than its existing holdings. Currently, our positive view of our portfolio companies means it's difficult to find stocks to sell to make room for new ideas. In our view, this indicates that the Fund's fundamental characteristics are more positive now than they have been for some time.

With respect to our broader outlook, we're encouraged by the shifting tone on inflation as we talk to the management teams of our companies. A year ago, nearly all our management discussions involved the tight labor market and the company's ability to pass on higher input costs. Both these issues have since moderated as supply chains have normalized and labor has become somewhat easier to find. At the same time, however, we still don't know what effect rising interest rates will ultimately have on the economy. Our response to these circumstances is to maintain a balanced portfolio with an emphasis on quality. We believe this approach is appropriate for a wide range of outcomes, from a "soft landing" for the economy to a larger-than-expected slowdown in growth.

Thank you for the opportunity to manage your assets.

Sincerely,

Jim Larkins and Austin Bone



## AVERAGE ANNUAL TOTAL RETURNS

FOR PERIODS ENDED JUNE 30, 2023

	Quarter*	1 Year	3 Years	5 Years	10 Years
Small Cap Value Fund—Investor	7.04%	17.71%	14.69%	6.02%	9.72%
Small Cap Value Fund—Institutional	7.08%	17.79%	14.83%	6.17%	9.84%
Russell 2000® Value Index**	3.18%	6.01%	15.43%	3.54%	7.29%
Russell 2000® Index†	5.21%	12.31%	10.82%	4.21%	8.26%

\*Returns less than one year are not annualized.

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Total Annual Fund Operating Expenses include operating expenses, including the management fee, before any expense reimbursements by the Advisor. **The Advisor has contractually agreed to limit certain expenses to 1.50% for the Investor Class and 1.05% for the Institutional Class through at least 1/31/2024.** See the prospectus for additional information regarding Fund expenses.

Wasatch Funds will deduct a 2.00% redemption fee on Fund shares held 60 days or less. Performance data do not reflect the deduction of fees or taxes, which if reflected, would reduce the performance quoted. For more complete information including charges, risks and expenses, read the prospectus carefully.

Investing in small cap funds will be more volatile and loss of principal could be greater than investing in large cap or more diversified funds. Investments in value stocks can perform differently from the market as a whole and from other types of stocks and can continue to be undervalued by the market for long periods of time. Investing in foreign securities, especially in emerging markets, entails special risks, such as currency fluctuations and political uncertainties, which are described in more detail in the prospectus.

**An investor should consider investment objectives, risks, charges and expenses carefully before investing. To obtain a prospectus, containing this and other information, visit [wasatchglobal.com](http://wasatchglobal.com) or call 800.551.1700. Please read the prospectus carefully before investing.**

The Wasatch Small Cap Value Fund's investment objective is long-term growth of capital. Income is a secondary objective, but only when consistent with long-term growth of capital.



*\*\*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.*

*Indexes are unmanaged. Investors cannot invest directly in these or any indexes.*

*The Wasatch Small Cap Value Fund has been developed solely by Wasatch Global Investors. The Wasatch Small Cap Value Fund is not in any way connected to or sponsored, endorsed, sold or promoted by the London Stock Exchange Group PLC and its group undertakings (collectively, the "LSE Group"). FTSE Russell is a trading name of certain of the LSE Group companies.*

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*The Index is calculated by or on behalf of FTSE International Limited or its affiliate, agent or partner. The LSE Group does not accept any liability whatsoever to any person arising out of (a) the use of, reliance on or any error in the Index or (b) investment in or operation of the Wasatch Small Cap Value Fund or the suitability of the Index for the purpose to which it is being put by Wasatch Global Investors.*

*"Fallen Angel" is a Wasatch term for a company with a solid long-term growth history and outlook whose current earnings have gotten off track.*

*"Undiscovered Gems" is a Wasatch term for companies that have little or no coverage by Wall Street analysts.*

## SMALL CAP VALUE FUND – TOP 10 HOLDINGS

AS OF MARCH 31, 2023

Security Name	Percent of Net Assets
Kadant, Inc.	4.2%
Ensign Group, Inc.	3.9%
Skyline Champion Corp.	3.3%
Innospec, Inc.	3.1%
Hamilton Lane, Inc. Class A	3.0%
Nova Ltd.	2.8%
Euronet Worldwide, Inc.	2.7%
Valvoline, Inc.	2.7%
Moelis & Co., Class A	2.6%
Grand Canyon Education, Inc.	2.6%
Total	30.8%
<i>Portfolio holdings are subject to change at any time. References to specific securities should not be construed as recommendations by the Fund or its Advisor. Current and future holdings are subject to risk.</i>	