

TOWLE & CO.

DEEP VALUE INVESTING

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Patiently waiting! The Towle portfolio is undervalued and out of favor. The valuation discrepancy between our deep value holdings and the general stock market doesn't add up. Based on consensus earnings estimates from Capital IQ, the median forward P/E for the Towle portfolio is 7.4x at quarter end. This translates to a forward earnings yield (return on investment) of 13.5% versus 7.4% for the Russell 2000 Value and 5.6% for the S&P 500. We believe a valuation gap of this magnitude is unsustainable.

Since the third quarter of 2018, the Towle Deep Value Composite (DVC) has dramatically underperformed the broader market. This nine-month period of lackluster results has been quite frustrating for us and surely disappointing for you, but our confidence in the long-term efficacy of our investment process is unshaken. We remain fully committed to our deep value discipline and believe an attractive long-term, capital appreciation opportunity has emerged.

Past performance is noted below. Results are annualized for periods greater than one year.

<i>Periods ending 6/30/19</i>	<i>Towle DVC (Gross of fees)</i>	<i>Towle DVC (Net of fees)</i>	<i>Russell 2000 Value</i>	<i>S&P 500</i>
3 months	-2.53%	-2.72%	1.37%	4.30%
6 months	9.94	9.56	13.47	18.54
1 year	-20.43	-21.08	-6.24	10.42
3 years	6.08	5.29	9.81	14.19
5 years	3.15	2.40	5.39	10.71
10 years	13.95	13.14	12.40	14.70
20 years	11.07	10.25	8.64	5.90
30 years	12.75	11.94	10.06	10.03
Inception (1/1/82)	15.28	14.46	11.67	11.65

*Returns are preliminary and subject to change. Past performance is no guarantee of future outcome.
Please refer to the last page for additional disclosures.*

Investment Environment

Though the U.S. investment landscape remains a mix of positives and negatives, overall, we see a favorable environment with low interest rates, subdued inflation, modest economic growth, and a 50-year low in the U.S. unemployment rate. Corporate credit conditions also remain supportive as investment grade and high yield credit spreads continue to contract. Looking more broadly, the St. Louis Fed Financial Stress Index, a wide-ranging measurement of financial stress across 18 different data sets, shows improving conditions and increasing liquidity. Additionally, as economic growth slows and U.S./China trade tensions linger, we believe the Fed will "act as appropriate" to sustain the expansion. If famed investor and financial analyst Marty Zweig were alive today, he would undoubtedly holler, "don't fight the Fed!" Considering these constructive conditions underpinning today's environment, we press on.

Portfolio Review

This section has been removed for compliance reasons to exclude discussing specific securities transactions.

Looking Ahead

Earlier this month, the U.S. economic expansion officially became the longest in our history, surpassing the 120 months of growth ending March 2001. The length of the current expansion has caused consternation among many market participants. But as top-ranked economist Nancy Lazar, the CEO of Cornerstone Macro, states, "It's not age that ends expansion. You die because you're fragile." (*Barron's*, May 20, 2019) Fortunately, "fragile" is not how she describes

current economic circumstances. In fact, she says U.S. growth remains sound and durable owing to productivity gains and tax reform.

Nancy's comments about economic expansions echo the market-related thoughts of Leon Cooperman, founder of Omega Advisors. "Bull markets do not die of old age, they die of excesses such as accelerating and above-trend economic growth, rapidly rising inflation, and interest-rate hikes from a hostile Federal Reserve." (*Fortune*, August 8, 2007) We have none of these issues. The economy is growing, though more slowly. Inflation is still below the Federal Reserve's 2% target. And the Federal Reserve is anything but hostile – indeed the next move in interest rates is expected to be down.

But will value investors like Towle & Co. participate? Greg Fisher, head of research at Gerstein Fisher, notes, "At some point, the cycle will likely turn and value will regain the upper hand. But it's hard to say when." (*Barron's*, April 8, 2019) Like Gregg, the Towle team knows not when this turn will commence. But we do know that the dispersion between high price-to-sales stocks and low price-to-sales stocks like the Towle portfolio exceeds even the Great Recession peak and is likely to mean revert. And as discussed at the opening of this letter, we also know that return on investment (earnings yield) remains a critical investment concept – one that has been productive for the Towle strategy over time.

As demonstrated many times in the past, we will stay steady, patiently awaiting events to take their natural course. The founder of Forbes magazine, B.C. Forbes, had a clear message to live by: "Refuse to be stampeded. Do your own thing." (*Forbes*, July 2017) We will adhere to B.C.'s advice.

Firm Update

Towle & Co. plans to open a second office in Denver later this year. We are in the process of identifying office space in the financial district of North Cherry Creek. Chris and James will work from the new location while Woody, Peter, and Wes, along with Joe Bradley and his team, will remain in St. Louis. Luke Barthelme will continue to work remotely from California. Over the last few years, we have invested heavily in our cloud-based IT infrastructure, developed a shared investment research platform, and implemented a fully-integrated compliance program that enable us to continue operating as a unified investment team across different sites. We are excited for the advantages this additional location will provide and hope you will come visit!

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DISCLOSURES

1) Performance results are calculated using a time-weighted total-rate-of-return method and are expressed in U.S. dollars. Results include the reinvestment of all income. Gross of fee performance is presented as supplemental information and reflects the deduction of all trading expenses, except in those accounts where ABP (Asset-Based Pricing) fees are assessed in lieu of standard trade commissions. Net of fee performance was calculated using actual management fees and ABP fees. 2) Although Towle & Co. makes no attempt to manage against the composition of a specific benchmark, the Firm provides the Russell 2000 Value Index as a readily accessible indicator of comparative small cap performance as well as the S&P 500 Index as a general indicator of the market at-large. The performance of an index is not an exact representation of any particular investment as one cannot invest directly in an index and investments made by Towle & Co. differ in comparison to the Russell 2000 Value Index in terms of security holdings and industry weightings. Towle & Co. invests in considerably fewer companies than either index with lower average multiples to book value, sales, earnings, and cash flow, and as a result, the volatility and returns of the indexes may be materially different from the individual performance attained by a Towle & Co. investor. 3) Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Unless otherwise noted, references to 'the Towle Portfolio' or 'the Portfolio' refers to a representative, fully discretionary portfolio managed in the Towle Deep Value strategy and member of the Towle Deep Value Composite. 4) Opinions expressed are those of Towle & Co. and should not be considered a forecast of future events or a guarantee of future results. Opinions and estimates offered constitute our judgment as of the date set forth above and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. All material presented is compiled from sources believed to be reliable, but no guarantee is given as to its accuracy. 5) CFA® is a designation issued by the CFA Institute. To earn the designation, candidates must pass three course exams, each requiring approximately 250 hours of self-study, and have completed four years of qualifying work experience.