Special Situations

Portfolio Update: Fourth Quarter 2019

The Special Situations strategy (the "Strategy") increased +4.93% gross of fees (+4.65% net of fees) during the fourth quarter of 2019, underperforming both the +9.94% and +9.07% returns of the Russell 2000 and S&P 500 Indexes, respectively. For the full year, the Strategy increased +31.94% gross of fees (+30.52% net of fees), outperforming the +25.53% return of the Russell 2000 and +31.49% return of the S&P 500.

	3 Months	YTD	1 Year	3 Years	5 Years	Since Inception (Annualized)
Special Situations Strategy	+4.65%	+30.52%	+30.52%	+4.65%	+7.07%	+11.36%
Russell 2000 Index	+9.94%	+25.53%	+25.53%	+8.59%	+8.23%	+11.83%
S&P 500 Index	+9.07%	+31.49%	+31.49%	+15.27%	+11.70%	+13.56%

Inception date: January 1, 2010. Performance is presented net of RMB Asset Management's maximum management fee and transaction costs. Performance is not net of RMB's Wealth Management advisory fee (if applicable). Please see important disclosures at the end of this document. Past performance is not indicative of future results, and there is a risk of loss of all or part of your investment.

We were disappointed with the Strategy's relative underperformance in the fourth quarter as we gave back a portion of its year-to-date performance, although the Strategy's performance still finished ahead of both benchmarks for the year. We also were extremely pleased with the absolute return generated in 2019, aided by the best year for the overall market since 2013. We'll opine later on the potential for the market in 2020, but (spoiler alert!) it will be nearly impossible to duplicate these level of returns. From a traditional attribution perspective, the Strategy's underperformance in the fourth quarter vs. the Russell 2000 was mostly driven by negative stock selection, with a modest negative contribution from sector allocation. The Technology sector was the standout in the quarter, as we didn't have much exposure to the fast-growing technology stocks that continued to perform very well in a "risk on" market environment. Along these lines, the biggest negative factor bet that led to the underperformance in the quarter was growth versus a more value-oriented portfolio. Performance was also hurt by our higher than normal cash balance. We sold some names that no longer had strong enough asymmetric risk-rewards in the third quarter and rather than replace that capital, choose to hold cash. Given the steady march higher of the market in the quarter, this decision served as a drag on performance by about 150bps. As a reminder, it's within the Strategy mandate to hold elevated levels of cash as an output of our disciplined investment process. While it's interesting to see drivers of performance over a three-month period, we remain focused on compounding shareholder capital over the long run, measured in years, not quarters

The fourth-quarter market environment saw a significant decrease in volatility, as optimism around a trade truce between the U.S. and China culminated with a preliminary agreement for a "phase one" deal in December. The market also responded positively to better monthly economic data and the ongoing tailwind of an accommodative Fed. Much of the recessionary and "late cycle" fears that were emerging mid-year were dampened down in the fourth quarter. The U.S. has remained one of the strongest and most resilient economies in the world over the past few years and consensus is for stable to potentially accelerating growth in 2020. The Manufacturing sector of the U.S. economy, which was hard hit by the impact of tariffs, could see some relief in coming quarters and growth comparisons should be relatively easy. The larger consumer-focused sector of our economy has remained strong with near full employment and some moderate real wage growth, particularly for the lower income consumer. The 10-year Treasury yield rose 24 basis points from 1.68% to 1.92% in the quarter. The Fed has signaled that it is done with its three 25 basis point rate cuts that it made in 2019 and is most likely to leave rates unchanged for the intermediate future, obviously dependent on any material changes in economic data. The impeachment inquiry of the president certainly has dominated the political headlines of late, but the stock market has largely shrugged it off as noise. That said, the highly charged political environment in DC and the potential for major tax and policy changes will remain part of the investment backdrop during this election year.

Third quarter earnings reports released in the fourth quarter saw revenues and earnings continue to surprise positively versus very low expectations, although there was minimal year-over-year earnings growth for the market as a whole. While the fourth quarter has yet to be reported, 2019 is likely to finish with very little earnings growth, likely 1-2% based on current expectations. Our message about overall equity valuations is similar with how we felt at the end of last quarter, and has only gotten worse given the further market run up. While not outlandishly expensive, we are not finding bargains to be abundant by any means, particularly in our quality growth universe. As mentioned in last quarter's letter, the Strategy is seeking a couple of strong new ideas and we did add one new name during the quarter, but attractively priced entry points in individual names with good fundamentals are hard to find. From a bottom-up, individual company perspective, the Strategy has more reward-to-risk ratios under one than it has greater than one. This was much different from where we stood at the end of 2018 after the big fourth-quarter selloff, which reflects the significant rebound in prices without any upward revisions in earnings estimates or growth expectations. The market return in 2019 came entirely from multiple expansion. From a longer-term perspective, even though the risk of a recession in the near term has likely diminished, we must be cognizant of the fact that we are likely in the late innings of a historically long positive economic cycle. With trade concerns diminishing and an accommodative interest rate environment, it's certainly possible that the macro-economic ballgame could easily continue into extra innings. As always, macro market predictions are very difficult to make with any hopes of being consistently accurate. We remain focused on bottom-up stock selection within a concentrated, yet diversified portfolio of companies with asymmetric risk/reward profiles.

Contributors and Detractors

Our largest contributor was Gardner Denver Holdings Inc., a manufacturer of flow control and compression equipment along associated aftermarket parts, consumables, and services to industrial, energy, and medical industries. The stock responded well despite a fairly weak third quarter earnings report, as the market has started looking forward to the combined earnings power that the company can generate after its merger with Ingersoll Rand's industrial business. This is the central component to our thesis on the name. The stock also benefited from better macro-economic data including a perk up in oil prices. Our second-largest contributor was cruise operator Royal Caribbean Cruises Ltd. The stock responded well as they reported a good third quarter and outlook, when excluding the short term disruptive impact of Hurricane Dorian. We continue to like Royal as a longer term holding, although acknowledge our original deep value investment thesis is getting a little long in the tooth.

Conversely, our biggest detractor was Plantronics Inc., a manufacturer of telephonic and video conferencing devices. This was last quarter's largest positive contributor, which shows how quickly fortunes can change. The stock declined after a horrible fiscal second quarter earnings report which negated our transformative acquisition thesis. We admitted our mistake and sold the name. Whole automobile auction provider KAR Auction Services Inc., a recent spinoff from Insurance Auto Auctions, was the second largest detractor. We sold the position after a weak third quarter report that suggested some longer-term problems with the move from physical auctions to on-line. We had a short time horizon on this investment thesis post spin-off, so acknowledged the mistake and exited.

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FOURTH QUARTER 2019 CONTRIBUTION REPORT
Ranked by Basis Point Contribution

	Basis Point Contribution	Return
Top Contributors		
Gardner Denver Holdings Inc.	+128	+29.65%
Royal Caribbean Cruises Ltd.	+111	+24.14%
Bausch Healthcare Companies Inc.	+100	+36.93%
Masco Corp.	+86	+15.51%
Tabula Rasa Healthcare Inc.	+66	+26.59%
Bottom Detractors		
Plantronics Inc.	-134	-34.64%
KAR Auction Services Inc.	-51	-15.74%
Six Flags Entertainment Corp.	-41	-9.50%
Viper Energy Partners LP	-32	-9.15%
Argo Group International Holdings Ltd.	-30	-5.96%

Past performance is not indicative of future results, and there is a risk of loss of all or part of your investment. The above does not represent all holdings in the Strategy. Holdings listed might not have been held for the full period. To obtain a copy of RMB's calculation methodology and a list of all holdings with contribution analysis, please contact your service team. The data provided is supplemental. Please see important disclosures at the end of this document.

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Portfolio Activity

TOP FIVE HOLDINGS AS OF 12/31/19	
Company	**% of Assets**
Masco Corp.	5.89%
PayPal Holdings Inc.	5.82%
Royal Caribbean Cruises Ltd.	5.42%
Gardner Denver Holdings Inc.	5.14%
Verra Mobility Corp.	4.85%

Holdings are subject to change. Strategy characteristics are intended to provide a general view of the entire portfolio, or Index, at a certain point in time. Characteristics are calculated using information obtained from various data sources. Past performance is not indicative of future results, and there is a risk of loss of all or part of your investment. The data provided is supplemental. Please see disclosures at the end of this document.

In the fourth quarter, the Strategy purchased three new names and also exited three holdings. We initiated positions in Tiffany & Co., Macquarie Infrastructure Corp., and Tabula Rasa Healthcare Inc. Tiffany, the iconic luxury goods retailer, was purchased on rumors that European luxury giant LVMH was interested in acquiring the company. We felt that the probability for a deal was reasonably high and the market price didn't fully reflect the price LVMH would likely have to pay. Our thesis subsequently played out in our favor as a deal was inked for a higher price. We hold the shares as of quarter end, but plan on liquidating them when we need the cash for other ideas. Macquarie Infrastructure was purchased immediately after the company announced it was exploring strategic alternatives. We had previously owned Macquarie in another RMB strategy, so were familiar with the business and portfolio of assets. We think there is demand for the three main infrastructure-related assets and the sum of the pieces in potential sale scenarios exceeds the current value of the stock. The company pays a 9% dividend while we wait for the thesis to play out. Tabula Rasa, a fast-growing provider of pharmaceutical software that aims to reduce the effects of adverse drug interactions on patients was added after the stock over reacted to a modest negative development in its third quarter earnings report. We think the customer issue is isolated and non-recurring, making the stock oversold with good recovery potential.

The three sell-offs in the quarter were Plantronics Inc., Fidelity National Financial Inc., and KAR Auction Services Inc. We previously discussed Plantronics and KAR and their negative impact on performance in the quarter. Title insurance provider Fidelity National was sold after the FTC disallowed its acquisition of competitor Stewart Title, which negated our thesis on the name. Fortunately, we had a nice positive return on the stock during our holding period due to a strong tailwind to growth in title insurance volumes from declining interest rates. This was our second ownership round in Fidelity, although each for different unique reasons and both proved to be profitable for the Strategy.

Outlook

U.S. corporate earnings growth, which is the biggest long-term driver of stock prices, was quite anemic in 2019. Once earnings are tallied up with the fourth quarter reports, the S&P is likely to have only grown earnings 1-2% in 2019. The outlook appears better for this year, with current Wall Street consensus for 10% earnings growth in 2020, although bottoms-up estimates are likely too high, with mid-single digit growth a more realistic number, in our opinion. It's not uncommon to see forward estimates be revised lower as individual companies give their annual outlooks with their year-end reports, an annual phenomenon that has occurred for the last several years. Given relatively easy comparisons, increased confidence in improving global economic growth and lower probability of recession, 2020 could be a much better year for underlying earnings growth. That said, we expect management teams to remain on the conservative side when setting forward expectations. The 31% market return this year was nearly all due to P/E multiple inflation, not from solid underlying earnings growth. With the market trading at 18.3x 2020 and 16.5x 2021, earnings estimates (which are probably still too high) versus a very long-term average around 16x, we still don't see a whole lot of margin of safety in valuations considering we're likely late cycle, particularly if earnings growth doesn't pick up this year. This view is consistent with our bottoms-up view on individual companies, both within the Strategy and potential new ideas. It's difficult to find a lot of high quality growth businesses selling at reasonable valuations today. As always, while we may opine on our view of the overall market, we do not pretend to have any ability to predicting where the market is heading in the short or intermediate term. It is a very difficult, if not impossible, task to add value via market timing, and we certainly didn't foresee how strong the market would be in the fourth quarter. We continue to focus the Strategy's efforts on owning companies with good growth prospects, strong economic moats, underleveraged balance sheets, superior management teams, and an ability to grow dividends. These are companies we believe can compound value for shareholders for years into the future. The opportunities to find high-quality, dividend growth companies selling at attractive valuations are becoming more abundant after the recent sell off, and we continue our "bottom-up" search to optimize the Strategy. Our disciplined investment process focuses more on individual company fundamentals and less on the overall market.

Given this letter brings us not only to the end of the year, but also the end of the decade we thought it might be worthwhile to reflect on what has transpired over the past 10 years. From the depths of despair in the Global Financial Crisis in 2008-2009, the U.S. has had an amazing run of improving prosperity over the last decade. This decade long run isn't just seen in the historically long economic expansion (first post war decade without a recession) and stock market returns (13.5% annualized) which, as wealth managers, tends to be our focus. There was an excellent short article in the December 17th edition of the Wall Street Journal entitled "The 2010's Have Been Amazing" that really put global accomplishments of the last decade in perspective. It's easy to get drawn into the daily media headlines that seem to be nothing but negative, but step back and take a longer point of view, and there is actually a lot of good news around the world to be reported that largely goes unnoticed because it changes so slowly. Worldwide declines in extreme poverty, improvements in human health and life expectancy, and progress on improving our environment were statistically global success stories in the last decade. There is reason to be optimistic that human ingenuity can continue to solve the major problems that it faces and life can get better from here. Heck, if the Chicago Cubs were able to win a World Series this decade, anything can happen! On this more optimistic note, we'd like to wish everyone a happy new year and a sincere thank you for the continued trust you place in us to manage your assets. If you have any questions, please do not hesitate to contact us.

Sincerely,

Todd M Griesbach

Todd Griesbach
Portfolio Manager

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RMB Asset Management

Special Situations Strategy // Annual Disclosure Presentation

Organization | RMB Capital Management, LLC ("RMB Capital") is an independent investment advisor registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940 and was established in 2005. The GIPS firm is defined as RMB Asset Management ("RMB AM"), a division of RMB Capital Management, LLC. Previously, the firm was defined as RMB Capital and was redefined on January 1, 2016 to only include the asset management business due to the difference in how its investment strategies and services are offered. RMB AM claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. RMB AM has been independently verified for the period April 1, 2005 through December 31, 2018. Verification assesses whether: (1) the firm has complied with all the composite construction are 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. Verification does not ensure the accuracy of any specific composite presentation. The Special Situations composite has been examined for the period of April 1, 2005 through December 31, 2015. The verification report and performance examination are available upon request. RMB AM maintains a complete list and description of composites, which are also available upon request.

Description | The Special Situations Strategy reflects the performance of fully discretionary equity accounts and is designed to capitalize on stock market inefficiencies in addition to conventional buy-and-hold strategies. "Special Situations" are defined as those that have extraordinarily favorable risk/reward characteristics and, for comparison purposes, are measured against the Russell 2000 and S&P 500 indices. The Special Situations Strategy Composite was created on January 1, 2010 and includes all accounts that are managed in accordance with the Special Situations investment strategy. The strategy evolved from a Small-Cap Investment Strategy which began January 1, 2008 and became the Special Situations Strategy on January 1, 2010. An account is included in the Composite on the first day of the first full month the account is under management. An account is removed from the Composite as of the last day of its last full month. Account performance is based on total assets in the account, including cash and cash equivalents. Results are based on fully discretionary accounts under management, including those accounts no longer managed by RMB. Valuations and returns are computed and stated in U.S. Dollars.

ANNUAL PERFORMANCE RELATIVE TO STATED BENCHMARK

		Composite Assets		Annual Performance Results								
Year End	Total Firm Assets as of 12/31 (M)	USD (M)	# of Accounts Managed	Composite Gross-of-Fees (%)	Composite Net-of-Fees (%)	Russell 2000 (%)	S&P 500 (%)	Composite 3-YR ST DEV (%)	Russel 2000 3-YR ST DEV (%)	S&P 500 3-YR ST DEV (%)	% Non-Fee Paying Assets	Composite Dispersion (%)
2018	4,196.9	43.3	143	-24.29	-25.14	-11.01	-4.38	16.44	15.79	10.80	1.45	0.61
2017	3,610.6	90.0	214	18.66	17.33	14.65	21.83	13.46	13.91	9.92	1.45	1.01
2016	3,047.5	76.5	206	15.44	14.07	21.31	11.96	15.84	15.76	10.59	0.15	0.87
2015	3,706.0	56.4	192	8.87	7.65	-4.41	1.38	13.74	13.96	10.47	0.17	0.62
2014	3,312.9	76.5	237	-4.95	-6.00	4.89	13.69	14.09	13.12	8.97	0.12	0.96
2013	3,248.5	89.8	259	21.77	20.40	38.82	32.39	15.74	16.45	11.94	0.20	0.81
2012	2,585.9	42.2	141	20.95	19.61	16.35	16.00	19.45	20.20	15.09	0.19	1.17
2011	2,218.0	27.5	80	6.05	5.60	-4.18	2.11	N/A	N/A	N/A	0.00	N/A
2010	1,881.9	0.2	2	47.16	45.71	26.86	15.06	N/A	N/A	N/A	0.00	N/A

**The 3-year annualized standard deviation is not presented for 2011 because 3-year monthly composite and benchmark returns are not available.*
***Composite dispersion is not presented for years where there are 5 or fewer portfolios in the composite for the full year.*

Fees *| Effective January 1, 2011, RMB' Capital's asset management fee schedule for this Composite is as follows: 1.25% on the first $250,000 in assets: 1.125% on next $750,000; 1.00% on next $2.0 million; 0.9% on next $2.0 million; 0.8% on next $5.0 million; 0.75% on next $15 million. Actual asset management fees charged by RMB may vary. Composite performance is presented on a gross-of-fees and net-of-fees basis and includes the reinvestment of all income. Gross-of-fees returns means it is net of transaction costs but gross of asset management fees, custodian fees and withholding taxes. The payment of actual fees and expenses would reduce gross returns. The compound effect of such fees and expenses should be considered when reviewing gross returns. The net returns are reduced by all actual fees and transactions costs incurred. The composite includes accounts that pay asset-based pricing for trading expenses. The maximum fee is 15 basis points per year; however, many accounts pay lower amounts due to household break-point relief. Returns for those accounts prior to 3/1/19 do not reflect the deduction of asset-based pricing, and are therefore gross of trading expenses. These accounts represent approximately 72% of composite assets. In addition to an asset management fee, some accounts pay a wealth management fee based on the percentage of assets under management to RMB Capital. The annual composite dispersion is an asset-weighted standard deviation calculated for the accounts in the Composite the entire year. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.*

Minimum Value Threshold *| There is no account minimum in the Special Situations Strategy.*

Comparison with Market Indices *| RMB compares its Composite returns to a variety of market indices such as the Russell 2000 and the S&P 500. These indices represent unmanaged portfolios whose characteristics differ from the Composite portfolios; however, they tend to represent the investment environment existing during the time period shown. An investment cannot be made directly in an index. The returns of the indices do not include any transaction costs, management fees, or other costs. The investment strategy and types of securities held by the comparison index may be substantially different from the investment strategy and types of securities held by your account in the Composite. Benchmark returns presented are not covered by the report of independent verifiers.*

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Other *| Past performance is not indicative of further results, and there is a risk of loss of all or part of your investment. Historical rates of return may not be indicative of future rates of return. Individual client performance returns may be different than the composite returns listed. Total Firm Assets as of 12/31 for the years 2010, 2011, and 2012 have been revised to exclude assets from personal trading accounts that were included in previously reported figures.*