



January 12, 2017

Dear Friends and Investors,

Stocks soared in Q4 following a stunning election upset that saw Republicans win the White House and retain a majority in Congress, resulting in a radical, pro-growth regime change in Washington. Following a weak start to the quarter, small cap stocks led the post-election rally as investors bet on lower taxes, increased infrastructure spending, and broad deregulation. **For 2016, small caps also outperformed large cap, delivering the best relative performance since 2010.**

From a style perspective, value handily outperformed growth across all market caps. Among small caps, **value outperformed growth by over +2,000 bps – the widest gap since the tech-bubble burst in 2001.** While volatility was low in 2016, the market did experience large price swings throughout the year. Leadership rotation among factors and sectors reflected this volatility. Ultimately, low beta and quality lagged for the year, which presented a headwind for River Road. Fortunately, **dividend payers outperformed providing a tailwind for several of our strategies.**

Overall, it was a very good year for River Road’s investment strategies. Despite factor headwinds and an extremely difficult period for most active managers, nearly all of our strategies outperformed their benchmarks – some significantly. Additionally, the two that fell short ranked well among their peers.

Composite Performance Summary ¹												
	Small Cap Value		Small-Mid Cap Value		Dividend All-Cap Value		Dividend All-Cap Value II		Focused Absolute Value®		Long-Short Equity	
	Q4	2016	Q4	2016	Q4	2016	Q4	2016	Q4	2016	Q4	2016
Gross	12.62%	28.48%	10.34%	27.35%	6.82%	21.47%	6.48%	20.96%	9.20%	27.14%	4.85%	6.14%
Net	12.41%	27.45%	10.16%	26.55%	6.68%	20.75%	6.38%	20.50%	9.11%	26.44%	4.57%	4.90%
Benchmark ²	14.07%	31.74%	9.34%	25.20%	7.24%	18.40%	7.24%	18.40%	7.24%	18.40%	2.14%	6.55%
+ / -	-1.45%	-3.26%	+1.00%	+2.15%	-0.42%	+3.07%	-0.76%	+2.56%	+1.96%	+8.74%	+2.71%	-0.41%

River Road’s **Focused Absolute Value® (FAV) Strategy** was firm champion in 2016, outperforming its benchmark by **+874 bps** (+804 bps net)! This marks seven of eight years that FAV has outperformed its benchmark (gross; six of eight years net). For Q4 and 2016, **stock selection was the primary driver of relative returns.** The Portfolio also benefited from the ability to move quickly and aggressively among market caps. FAV increased its weighting in small caps earlier in the year, which contributed **+177 bps** of relative return for the quarter and **+447 bps** for 2016.

River Road’s **Dividend All-Cap Value Strategies** (DAV and DAV II) trailed the benchmark in Q4, but outperformed for 2016. **Stock selection was largely responsible for the outperformance, but sector allocation was also modestly positive for the year.** In a reversal from recent years, dividend stocks performed relatively well in 2016. The Strategy’s bottom-up, value-focused investment process also provided the means to navigate a relatively treacherous shift from defensive to cyclical leadership within the dividend universe, **which further aided in the Strategy outperforming a large majority of its peers.**

River Road’s **Small Cap Value (SCV)** and **Small-Mid Cap Value (SMID) Strategies** delivered similar absolute returns for 2016, but varied in their relative performance. **SMID outperformed its benchmark for both Q4 and 2016**, with performance driven by strong stock selection, particularly among the Strategy’s Industrials holdings. Conversely, SCV outperformed SMID but lagged the benchmark for both periods. **SCV’s underperformance in Q4 occurred during the post-election period**, when the index rallied **+17.41%** and the Composite returned **+14.27%** (+14.10% net). During this period, the primary driver of underperformance was a significant underweight to Banks & Thrifts (contributing **-191 bps**).

SCV’s relative underperformance in 2016 is disappointing given **the Strategy led the index throughout much of the year and benefited from a near-record seven M&A events.** The Strategy also performed very well relative to its peers. The Strategy’s lagging performance can be attributed to a few factors, including an elevated cash level (**-247 bps**) and an

¹ Please see the attached disclosures. Past performance is no guarantee of future results.

² Benchmarks: SCV – Russell 2000 Value; SMID – Russell 2500 Value; DAV – Russell 3000 Value; DAV II – Russell 3000 Value; FAV – Russell 3000 Value; Long-Short Equity – 50% Russell 3000 index/50% BofA Merrill Lynch U.S. T-Bill 0-3 month index.



underweight allocation to **Banks & Thrifts (-180 bps)**. Most investors are probably unaware Banks and Thrifts, which tend to be a highly correlated group, are both trading near all-time high valuations and **represented an astonishing 25% of the benchmark index at year end**. From the team's perspective, unless banks benefit from significant interest rate hikes, much stronger loan growth, lower corporate taxes, **and** significant deregulation, they represent a highly speculative risk in the index that the team hopes to leverage through the Portfolio's underweight position in the months ahead.

The **Long-Short Equity Strategy** performed in line with the benchmark return (50% R3000 Index / 50% BofA Merrill Lynch U.S. T-Bill 0-3 month index) during what proved to be a challenging period for many hedged equity managers. **Strong stock selection in the long portfolio drove the 2016 results**. The Strategy's 'Drawdown Plan' did weigh on performance due to the January market swoon and abrupt rebound, but **this innovative feature of the Strategy is considered critical to achieving the Portfolio's maximum drawdown objective of -15%**.

We are pleased to report a significantly lower fee structure for the Long-Short Equity Strategy. While the prior fee structure was highly competitive amongst its peers, **we believe the liquid alternative space is improperly priced and want to lead what should be a much broader pricing reform within the category**.

With regard to firm news, **there were no material developments in the fourth quarter**. This allowed the team to remain focused on navigating the post-election rally and the challenges posed by lofty stock valuations. This February, our leadership team (a rather broad group stretching across all functions within the firm) will conduct an offsite meeting to **review industry trends, firm and product strategy, investment processes, new initiatives, and long-term objectives**. We host such gatherings every few years and, with all of the changes occurring in our industry, it promises to be an engaging event for all.

We would like to recognize our Chief Operating Officer & Chief Compliance Officer, Thomas D. Mueller, CFA, CPA, for winning the firm's internal simulated stock picking competition. The competition had four stages that stretched over two years and included all River Road associates and interns. It was primarily developed to better engage the firm's non-investment personnel with River Road's investment team and processes. **Tom earned a decisive victory, having not only the highest point total from all four segments, but the highest average total relative return (by a wide margin)**. It was an impressive and well-deserved victory.

Finally, at the beginning of each New Year we like to reiterate to you, our associates, and business partners our pledge to **pursue investment excellence with passion and discipline; continue investing in our firm, associates, and portfolios; and always maintain the unique culture and values we embraced on the day we founded River Road**.

We hope you enjoy reading River Road's portfolio commentary and outlook and welcome your questions and feedback.

R. Andrew Beck
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Senior Portfolio Manager*

James C. Shircliff, CFA
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Disclosures:

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For all composites, the U.S. dollar is the currency used to express performance and performance includes the reinvestment of income.

Small Cap Value Composite Disclosures:

Inception date: January 1, 1998. The composite contains fully discretionary accounts that seek capital appreciation by investing primarily in small cap value domestic equity securities that trade at a discount to our assessed valuation as determined using RRAM's proprietary Absolute Value® approach. For this composite, RRAM defines a small cap company as one whose market capitalization is less than \$3 B. The Manager selects securities from a universe of companies with a market capitalization at the time of initial purchase typically between \$50 MM and \$3 B, employing a value-driven, bottom-up fundamental approach. The official benchmarks for the Small Cap Value Equity Composite are the Russell 2000 Value and Russell 2000.

As of December 31, 2016, net of fees returns for the Small Cap Value Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, 10 year, and Inception to Date periods: 4.52%, 12.41%, 27.45%, 27.45%, 8.23%, 13.64%, 6.02%, and 10.68%. As of December 31, 2016, returns for the Russell 2000 Value are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, 10 year, and Inception to Date periods: 4.13%, 14.07%, 31.74%, 31.74%, 8.31%, 15.07%, 6.26%, and 8.66%.

Performance presented prior to April 1, 2005 occurred while the original members of the Portfolio Management Team were affiliated with a prior firm and those Portfolio Management Team members were the only individuals primarily responsible for selecting the securities to buy and sell. A review of this track record for compliance with portability requirements of the GIPS® standards was conducted by Ashland Partners & Company.

Small-Mid Cap Value Composite Disclosures:

Inception Date: March 1, 2007. The composite contains fully discretionary accounts that seek capital appreciation by investing primarily in small-mid cap value domestic equity securities that trade at a discount to our assessed valuation as determined using RRAM's proprietary Absolute Value® approach. For this composite, RRAM defines a small to mid-cap company as one whose market capitalization is less than \$10 B. RRAM selects securities from a universe of companies with a market capitalization at the time of initial purchase typically between \$250 MM to \$10 B, employing a value driven, bottom-up fundamental approach. The official benchmark of the Small-Mid Cap Value Composite Portfolio is the Russell 2500 Value.

As of December 31, 2016, net of fees returns for the Small-Mid Cap Value Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 3.38%, 10.16%, 26.55%, 26.55%, 7.62%, 13.30%, and 6.78%. As of December 31, 2016, returns for the Russell 2500 Value are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 2.85%, 9.34%, 25.20%, 25.20%, 8.22%, 15.04%, and 6.85%.

Dividend All-Cap Value Composite (DAV) and Dividend All-Cap Value II Composite (DAV II) Disclosures:

Inception Date DAV: October 1, 2003. Inception Date DAV II: January 1, 2011. The composites contain fully discretionary accounts that seek to provide long term capital appreciation and high current income by investing primarily in a diversified, all-cap basket of income producing equity securities that trade at a discount to our assessed valuation as determined using RRAM's proprietary Absolute Value® approach. The composites are primarily invested in dividend-paying common stocks. The composites may also be invested in a broad range of foreign stocks, publicly traded partnerships, convertible preferred stocks, Real Estate Investment Trusts ("REITs"), investment companies, and royalty income trusts. For the DAV II Composite only, the securities must have a market capitalization of typically at least \$1 B at the time of initial purchase. RRAM employs a value-driven, bottom-up approach. The official benchmark for the composites is the Russell 3000 Value.

As of December 31, 2016, net of fees returns for the Dividend All-Cap Value Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, 10 year, and Inception to Date periods: 2.08%, 6.68%, 20.75%, 20.75%, 8.35%, 13.10%, 7.48%, and 11.06%. As of December 31, 2016, returns for the Russell 3000 Value are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, 10 year, and Inception to Date periods: 2.63%, 7.24%, 18.40%, 18.40%, 8.55%, 14.81%, 5.76%, and 8.81%.

Performance presented prior to April 1, 2005 occurred while the original members of the Portfolio Management Team were affiliated with a prior firm and those Portfolio Management Team members were the only individuals primarily responsible for selecting the securities to buy and sell. A review of this track record for compliance with portability requirements of the GIPS® standards was conducted by Ashland Partners & Company.

As of December 31, 2016, net of fees returns for the Dividend All-Cap Value II Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 1.92%, 6.38%, 20.50%, 20.50%, 8.59%, 13.02%, and 11.86%. As of December 31, 2016, returns for the Russell 3000 Value are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 2.63%, 7.24%, 18.40%, 18.40%, 8.55%, 14.81%, and 12.18%.

Long-Short Equity Composite Disclosures:

Inception date: July 1, 2010. The composite contains a fully discretionary account that seeks equity-like returns with reduced volatility over a full market cycle by investing primarily in long equity securities that trade at a discount to our assessed valuation and selling short equity securities that trade a premium to our assessed valuation as determined using RRAM's proprietary Absolute Value® approach. The composite will invest in short securities. The long and short portfolios will typically represent 50-100% and 10-90% of the total composite, respectively. Additionally, the composite may use options, futures, and other derivatives but these will not represent a significant portion of the composite. The official benchmarks for the composite are the Blended Index and the Russell 3000. The Blended Index was added as a benchmark effective 10/31/2016. The Blended Index represents a 50% weighting of the Russell 3000 Index and a 50% weighting of the BofA Merrill Lynch U.S. T-Bill 0-3 Month Index; rebalanced daily.

As of December 31, 2016, net of fees returns for the Long-Short Equity Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: -0.52%, 4.57%, 4.90%, 4.90%, 1.23%, 6.27%, and 7.90%. As of December 31, 2016, returns for the Russell 3000 are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 1.95%, 4.21%, 12.74%, 12.74%, 8.43%, 14.67%, and 15.08%. As of December 31, 2016, returns for the blended index (50% R3000 Index / 50% BofA Merrill Lynch U.S. T-Bill 0-3 month index) are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 1.00%, 2.14%, 6.55%, 6.55%, 4.43%, 7.36%, and 7.65%.

Focused Absolute Value® Composite Disclosures:

Inception Date: January 1, 2009. **The team of analysts involved with recommending investments for Focused Absolute Value® has changed and may continue to change over time.** The portfolio managers may not have historically approved all trades prior to execution. Fully invested is as defined by RRAM and this standard may change over time. Prior to September 30, 2014, the composite was known as the Research Fund Composite.

The composite contains fully discretionary accounts that seek capital appreciation by investing primarily in equity securities that trade at a discount to our assessed valuation as determined using RRAM's proprietary Absolute Value® approach. For this composite, RRAM selects securities from a universe of companies that are held by other RRAM strategies, which typically includes all market capitalizations. RRAM employs a value-driven, bottom-up fundamental approach. One client account is a current employee of RRAM. The official benchmark for the composite is the Russell 3000 Value. Fully invested is as defined by RRAM.

As of December 31, 2016, net of fees returns for the Focused Absolute Value® Composite are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 0.67%, 9.11%, 26.44%, 26.44%, 10.06%, 16.90%, and 19.07%. As of December 31, 2016, returns for the Russell 3000 Value are as follows for the month, QTD, YTD, 1 year, 3 year, 5 year, and Inception to Date periods: 2.63%, 7.24%, 18.40%, 18.40%, 8.55%, 14.81%, and 13.60%.

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