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INVESTMENT STRATEGY OUTLOOK – SMALL CAP EQUITY

December 31, 2015

The FMI Small Cap portfolios gained approximately 1.4% in the December quarter compared to 3.59% for the benchmark Russell 2000 Index. Sectors that helped included Retail Trade, Producer Manufacturing and Health Services. Stocks that gained in the period included Woodward, Allscripts, and Avery Dennison. Finance, Health Technology and Technology Services were all sectors that detracted in the quarter. Our regional banks, Zions and Cullen/Frost, were both hurt by energy loans. Greenlight Capital suffered from a rash of poorly performing investments. Ryder continued to execute well fundamentally, but worries about the economy pounded the stock. Our underweighted position in both Health Technology and Technology Services detracted meaningfully in the December quarter. Year-to-date, the commodity-related, cyclical and heavier industrial stocks continued to decline sharply, while many of the more defensive names gained or held ground. Valuation has mattered little over the past several years, and especially in 2015. Growth stocks continued to outpace value stocks; these cycles are painful for value investors but they have historically turned. We remain disciplined in our approach and believe the aforementioned poorly performing stocks are trading at a discount to their true worth.

Despite making very satisfactory absolute returns during this cycle, value investors are indeed frustrated. The market that has existed over the better part of a decade has rewarded growth (or cross-your-fingers growth in the case of the biotechs) and penalized value, at least on a relative basis. This has occurred across the spectrum, regardless of market capitalization or geography, and in both developed and undeveloped markets. The table below shows value and growth benchmarks over various time frames; it is sobering to see how long value investors have wandered through the proverbial desert.

Seven years of suppressed interest rates have helped turn the traditional relationships and dynamics between value and stock performance upside down. Since 1926 (the earliest date wherein rigorous stock price information has been collected), the cheapest stocks have handily outperformed the more expensive ones. Nearly every study of long-term investment performance demonstrates the same thing: value trumps growth. But over shorter periods of time, growth sometimes beats value. *Barron's* recently cited data from Dartmouth professor Kenneth French showing that the cheapest stocks in the U.S. have lagged their more expensive counterparts since February of 2007, the longest losing streak ever chronicled. The fourth quarter of 2015 exhibited this in spades.

Total Returns Through 12/31/15

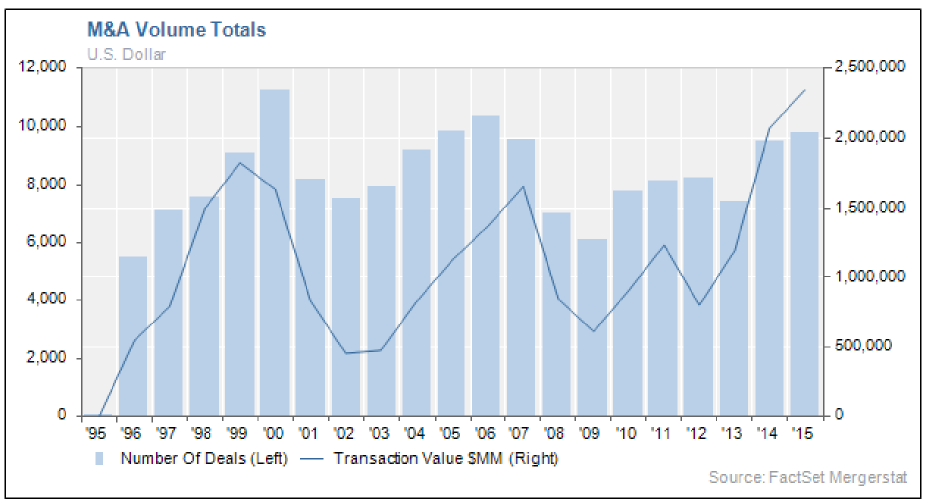
	1 yr.	3 yr.	5 yr.	10 yr.	15 yr.
Russell 1000 Value Index	-3.8%	44.6%	70.6%	81.7%	135.1%
Russell 1000 Growth Index	5.7%	59.5%	88.6%	126.8%	89.0%
Value Underperformance	***-9.5%***	***-14.9%***	***-18.0%***	***-45.1%***	***46.1%***
Russell 2000 Value Index	-7.5%	29.7%	44.7%	72.0%	224.8%
Russell 2000 Growth Index	-1.4%	49.2%	66.0%	114.9%	140.6%
Value Underperformance	***-6.1%***	***-19.5%***	***-21.3%***	***-42.9%***	***84.2%***
MSCI EAFE Value Index	-4.9%	12.5%	18.3%	32.2%	92.6%
MSCI EAFE Growth Index	4.6%	23.7%	28.3%	56.7%	76.8%
Value Underperformance	***-9.5%***	***-11.2%***	***-10.0%***	***-24.5%***	***15.8%***
MSCI World Value Index	-4.0%	28.2%	42.2%	58.3%	100.1%
MSCI World Growth Index	3.5%	40.5%	55.8%	89.8%	94.9%
Value Underperformance	***-7.5%***	***-12.3%***	***-13.6%***	***-31.5%***	***5.2%***
MSCI Emerging Markets Value Index	-18.6%	-25.9%	-29.5%	39.6%	281.2%
MSCI Emerging Market Growth Index	-11.3%	-11.8%	-13.9%	44.7%	203.1%
Value Underperformance	***-7.3%***	***-14.1%***	***-15.6%***	***-5.1%***	***78.1%***

Source: Bloomberg

Many investors have capitulated on value strategies and jumped on the growth and momentum bandwagon; this is reflected in a couple of ways. First, a huge amount of money continues to flow into passive investment vehicles that are primarily designed to chase growth (e.g. healthcare, biotech) or mimic the benchmarks like the S&P 500 or Russell 2000 Indices. Because the benchmarks are market cap-weighted, they benefit from this momentum trade. Through November, Morningstar reports that $173 billion has moved into long-term passive funds this year. Of course, the flipside is heavy outflows from active managers. Second, the market narrows as the underlying economy remains tepid and fewer companies exhibit growth. Year-to-date through December 7, 2015, 1% of the S&P 500, or just five stocks -- Amazon, Alphabet/Google, Microsoft, Apple and Facebook -- accounted for essentially all of the then positive (+2.9%) performance of the Index. The bottom half of the index was down nearly 7%. It is reminiscent of the 1990s market, which also narrowed considerably in the run-up, with stocks such as Cisco, Intel, Dell and Oracle getting the lion's share of attention.

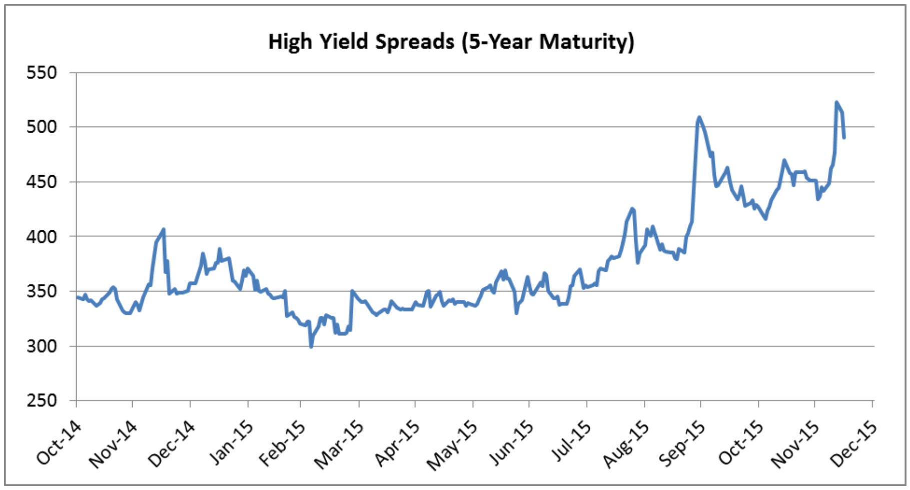
In the 1990s, the S&P 500, Russell 2000 and Nasdaq Composite Indices had compound annual returns of 18.2%, 13.4% and 24.5%, respectively. This compares to the long-term average return of approximately 9-10%. There is a gross misperception in the marketplace that exchange traded and index funds are somehow less risky than "active" management. In the 3-year period following the peak in early 2000, these indices lost approximately 40.9%, 29.5%, and 70.4%, respectively.[1] In the current bull phase, extending roughly 80 months from March of 2009 through this November, the S&P 500, Russell 2000 and Nasdaq Composite have compounded at 17.9%, 18.5% and 21.3%, respectively. Fewer and fewer names are participating as momentum investors pile into the stocks that are "working" and vacate the disappointing ones. Because value managers are losing assets, they have less ability to keep the unpopular stocks from losing even more value. It is a classic negative spiral that historically reverses in tough markets.

Today's stock market is also characterized by a surge in deal activity. Pfizer-Allergan and Dow Chemical-DuPont were the latest blockbuster announcements. We described a number of big, expensive deals in the June letter. According to Dealogic, mergers and acquisitions (M&A) activity surpassed $5 trillion for the first time ever in 2015. Seeking the deal rather than organic investment has been the hallmark of this cycle, and it reflects the misallocation of resources that takes place in an artificially low interest rate environment. CEOs can justify a 5% return on invested capital (ROIC) deal when borrowing at 3%. That this return is below any normalized cost of capital is apparently inconsequential to today's managers and the stock market, at least in the short run. The debt that has been layered on over the past half-decade will be there in the next recession, or when it is time to refinance; it seems highly unlikely that the interest rate environment will be nearly as hospitable then as it is today. Today's M&A-driven stock market -- featuring companies like Valeant, Danaher, Kraft-Heinz and Newell -- harkens back to the 1960s, a period when the market was fueled by multi-sector acquisition companies like Litton, ITT and Gulf & Western. In mid-December, Newell announced a bid for Jarden, which is itself a product of dozens of acquisitions. Jarden has been a big winner over the past five years on Wall Street, despite an ROIC that has averaged 6.2%. Debt has grown at more than double the rate of operating income growth; that will be Newell's issue down the road. These speculative periods rarely end well. 2014-2015 should go down as one of the most active M&A periods ever, as depicted above.



[1] The S&P 500 peaked on March 21, 2000; we have selected the three years beginning March 31, 2000.

The deal market feeds the debt market, and that area -- at least in the noninvestment grade sector -- has recently taken it on the chin. Historically, this market has been the proverbial canary in the coal mine, although the collapse in energy prices is certainly a much bigger factor today in the high-yield space. Nonetheless, spreads have blown out, as depicted in the chart to the right. What is most fascinating about this market is how a smallish ($788 million) fund from Third Avenue could essentially seize up in early December. The fund, facing severe liquidity problems, engaged in some maneuvers that essentially prevented investors from redeeming shares while attempting to liquidate the strategy with best efforts. Third Avenue was not the only junk bond fund to get in trouble this cycle; at least one other player that we know of, a hedge fund named Stone Lion Capital Partners, suspended redemptions on December 11, 2015. The two co-founders of Stone Lion were… (drumroll please) the former co-heads of the Distressed Debt and High Yield trading group at Bear Stearns when it blew up eight years ago! When we talk with traders, the overwhelming sentiment is that there is precious little liquidity, not just in the high-yield area, but also across the spectrum of equity markets. Liquidity will get a lot more airtime if equity markets get bumpier.



The lack of liquidity, combined with disappointing fundamentals in the cyclicals and commodity-related sectors, has resulted in a growing number of significantly declining stocks. While many of these equities started at very high valuations and now may only be “reasonable,” we have been very busy getting up-to-speed on a large number of them. So far, many of the inexpensive issues reside in the heavier industrial, energy and agricultural areas, where we have already made selective additions. There is no way to be certain about the economic trajectory today, so prudence dictates a measured approach to being contrarian. Clearly, a strong dollar, combined with weakness in China, Brazil and Europe, has had a very negative impact on the fundamentals of a great many industrial and commodity-related companies. They appear to be in their own recession as 2015 ends, and we do not know if it will spill over to the rest of the economy in 2016. An Institute for Supply Management number that dropped below 50 in November signals contraction. The Fed’s 0.25% hike of the Fed Funds rate is their way of saying the economy is out of the woods, but with 2% GDP growth in the third quarter, and the December quarter looking weak, it certainly doesn’t feel that way. Sales and earnings growth across the aggregate of corporate America shows very little growth or even contraction, depending on whose numbers are used.

Without a doubt 2015 was a tough year for FMI, and value investors as a whole. We have had some poor stocks, and our style and disposition kept us away from the stocks that have been winning; it is against our constitution to chase expensive stocks. We also misjudged the market’s willingness to pay up for growth and penalize disappointments, which makes some of our contrarian bets look bad in the short run. Many highly respected long-term value managers that we view as our competition have seen the same thing in 2015 and over the past several years; misery loves company. These cycles are never fun to go through, but we are confident that buying solid businesses at attractive prices is a winning strategy for the long haul.

Thank you for your confidence in Fiduciary Management, Inc.

Fiduciary Management Inc.
Small Cap Equity Composite
12/31/2004 - 09/30/2015

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation		Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
						Composite	*Benchmark			
2005	11.12	10.26	4.55	186	0.69	n/a	n/a	$ 1,605.8	$ 3,174.4	50.59%
2006	18.46	17.56	18.37	147	0.73	n/a	n/a	$ 1,606.8	$ 3,589.4	44.77%
2007	-0.92	-1.72	-1.57	161	0.85	n/a	n/a	$ 1,520.2	$ 3,960.4	38.39%
2008	-21.06	-21.69	-33.79	145	1.16	n/a	n/a	$ 1,212.4	$ 4,062.5	29.84%
2009	35.72	34.56	27.17	165	0.97	n/a	n/a	$ 2,004.6	$ 7,008.9	28.60%
2010	23.45	22.43	26.85	170	0.48	n/a	n/a	$ 2,477.7	$ 9,816.0	25.24%
2011	5.64	4.79	-4.18	179	0.34	21.17%	24.99%	$ 2,523.2	$ 12,273.6	20.56%
2012	11.34	10.43	16.35	182	0.40	15.46%	20.20%	$ 2,609.5	$ 15,253.5	17.11%
2013	33.43	32.33	38.82	180	1.04	12.51%	16.45%	$ 2,801.8	$ 19,705.3	14.22%
2014	7.99	7.06	4.89	178	0.39	9.65%	13.12%	$ 3,006.5	$ 21,001.1	14.32%
Q1 2015	2.68	2.46	4.32	181	0.17	10.08%	13.23%	$ 3,023.0	$ 21,939.0	13.78%
Q2 2015	-1.36	-1.56	0.42	178	0.12	9.08%	12.33%	$ 2,939.5	$ 22,136.3	13.28%
Q3 2015	-8.16	-8.36	-11.92	171	0.25	10.07%	13.41%	$ 2,672.7	$ 20,632.7	12.95%

*Benchmark: Russell 2000 Index®

Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Inc. (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 09/30/2015. Verification assesses whether (1) the firm has complied with all the composite construction 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. The Small Cap Equity composite has been examined for the periods 12/31/1993 -09/30/2015. The verification and performance examination reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $20.6 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The FMI Small Cap Equity Composite was created in January 1980. These accounts primarily invest in small to medium capitalization US equities.

The FMI Small Cap Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts, with a market value greater than $500,000 as of month end. A small percentage of composite assets (typically ranging from 0-5%) historically has been invested in unmanaged fixed income securities at the direction of account holders. From December 31, 1993 thru September 30, 2002 all accounts included were managed for at least one quarter, from October 1, 2002 to present all accounts were managed for at least one month. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes. Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2011, the trailing three year annualized ex-post standard deviation for the Composite and Benchmark are required to be stated per GIPS®.

Currently, the advisory fee structure for the FMI Small Cap Equity Composite portfolios is as follows:

Up to $25,000,000	0.90%
$25,000,001-$50,000,000	0.85%
$50,000,001-$100,000,000	0.75%
$100,000,001 and above	0.65%

The firm generally requires a minimum of $3 million in assets to establish a discretionary account. High Net Worth individuals may establish an account with a minimum of $1,000,000, however, the firm reserves the right to charge a minimum dollar fee for High Net Worth individuals depending on the client servicing involved. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request.
Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The Russell 2000 Index® measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000® Index representing approximately 8% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. The Small Cap Equity composite uses the Russell 2000 Index® as its primary index comparison.