

Riverwater Partners Q1 2026 Webinar Transcript
Auto-Generated Captions (Vimeo) — Cleaned & Formatted

MATT DRVARIC — Introduction & Firm Update

Welcome to the Riverwater Partners first quarter 2026 webinar. My name is Matt Drvaric, and I'll be your host for today's call. All participants are currently in listen-only mode. If you'd like to submit a question, please use the questions box located at the bottom of your control panel. Please note that today's event is being recorded, and a replay will be made available following the webinar.

Let's begin with an overview of today's agenda. This afternoon, we'll start with a brief firm update. Adam Peck, our co-founder and chief investment officer, will discuss the small cap market environment and review performance for the sustainable value strategy. Following, Nate Fredrick, portfolio manager, will provide a performance update on our small cap strategy. To close, Cindy Bohlen, our director of responsible investing, will review highlights from our recently published 2025 sustainability report. After the presentations, we'll address any questions.

Riverwater offers three concentrated small cap-oriented strategies. Each strategy is guided by the same philosophy, process, investment team, and differentiated primarily by valuation discipline and market cap focus. I'm proud to announce that our flagship strategy, the sustainable value product, broke the 100 million asset mark in the quarter. Additionally, we are excited about the small cap strategy, which ended the quarter with nearly 80 million in assets and was included in the recently launched Acuitas Small Cap Active ETF, ticker AMES.

We remain energized by the opportunities ahead in both strategies and are grateful for the trust you place in us each day. I'll turn it over to Adam, who will share commentary on the small cap market.

ADAM PECK — Small Cap Market Environment

Great. Thank you, Matt, and thank you all for joining us.

Just going back to 2025, as you should all be aware, it was a very tough market for quality managers as it was driven by negative earners with low returns on capital. And we started to see low quality start to fade very late in '25. But interestingly enough, in the first quarter, that low quality rally has been replaced by a hyper-concentrated rally, as seen in the slide here.

And what this slide depicts is the contribution of the top 5, 10, 25, and 50 stocks in the Russell 2000 returns. And you can see the most recent quarter is the orange bar. Just in the last quarter, the top five stocks represented over 100% of the Russell's return compared to an

average of usually 14% to 15% of return of the top five stocks. And same thing with the top 50 stocks were an incredible 447%.

On the next slide, I show the exact same data, but it's over a time series. And so on that slide, what it is depicting is quarters where the Russell 2000 was up about 0.75% to 7.5%. And if you go back to 1986, there have been 21 negative quarters since 1996 and 13 double-digit positive quarters since 1986. And so if you remove those large divergences, this range represents 80% of all quarters. And so again, we're off the charts for concentration. We blow past the last peak. We blow it out of the water, which funny enough, was around the year 2000, the tech bubble, when you had another life-changing technological event, and we have another one today, which is AI.

And what's interesting is that it's been hyper imperative in this market to be in the best performing small caps to keep up. So, on the next slide, while the statement I'm going to make is not based on statistical significance, I will say that the last time small caps were as super concentrated as they are today marked the last turning point for small cap dominance versus large caps.

So the blue line here goes back to 1925 and represents the relative performance of small caps versus large. So if the line is going up, small caps are outperforming. If the line is going down, large caps are outperforming and, not surprisingly, small caps are underperforming. And I think you can blame me, but I basically got into the small cap industry at the absolute peak of small caps performance, and so it's been downhill for me on a relative basis.

But again, going back to the 1999, 2000 timeframe is when small caps really started their run. And you can see this relationship is inherently cyclical. Since World War I, small cap relative performance has not dropped meaningfully below one on a relative basis. And so what else other than just a time series could give me confidence that the cycle is turning?

And that would be the data on the next slide, which is last quarter. So last quarter, small caps outperformed by 5.2% versus large, in what was a very volatile quarter, and it was the largest outperformance by its margin since the first quarter of 2021. And we've only seen this large margin beat a handful of times in the last 20 years. And we haven't seen back-to-back beats, small versus large, over the last eight years. So really, we're due.

And small is attractive, as I've discussed on other webinars, on both a historical valuation basis and a relative growth basis. So we think small has a very good setup.

Speaking of the types of small that you want to invest in, we think the setup for quality small caps is very sound as well. This chart compares the relative valuation on cash flows of Russell 2000 stocks in the S&P 600, which another way to say it is high-quality stocks, because the S&P 600 requires all companies to have historical profitability, to all other stocks in the Russell 2000. So when the blue line is going down, quality is underperforming. When it's going up,

quality is outperforming, and it's traded in a range. It's now trading at a very low range compared to historical valuations, and it's a two standard deviation event. So we think the setup is very strong for quality.

And on the next slide, we don't think anyone has missed the boat on the small cap rally. So we think there's plenty of runway left for small, because the bull market, going back to, I call it Liquidation Day, but most people call it Liberation Day, for tariffs last year, the small cap bull market is only one year old. So, we overshot to the upside this past January, when small caps had a huge January effect and were up double digits in a week or two. But March then over-corrected with the excursion in the Middle East. And so we believe where we are today leaves higher than average upside compared to historical bull markets.

And what's been driving this bull market? As everyone knows, it's AI. So, nothing shocking to share here. I just thought this was a pretty interesting chart from MIT that just shows what projected electricity demand would be. When I think about the US economy, I shudder to think what it would look like if we didn't have a trillion-dollar AI CapEx drive going. But what gives me some confidence is that the hyperscalers continue to increase their CapEx in AI. And based on my knowledge of where most companies are, private companies, small cap companies, I'd say all companies are really early in their AI journeys. So I do believe the demand for AI is going to continue.

And so I do have faith that these electricity numbers are at least directionally right. And this is showing that electricity demand should triple in the next five years. And so as small cap investors, we take a picks and shovels approach, and have AI-driven themes across a broad swath of our portfolio and in multiple sectors. And AI has carried a lot of our returns.

But I will say we're very cognizant of stock prices, which can often disassociate from reality, either to the downside or to the upside. And we're seeing a lot of signs that there's probably the beginning innings of too much euphoria in the AI trade. Yesterday, an AI-focused chip manufacturer went public way above its stated range, and I think it opened up more than 100%. It got halted. If anyone is old enough to remember 1999, it's kind of what we saw then.

So, just to finish up here, I will say our performance has probably been driven by AI themes, but we're becoming overall net sellers of the AI stocks we own. And we'll get into that into some detail as we hit the portfolio. So with that, I will pass the baton over to Nathan.

NATHAN FREDRICK — Small Cap Strategy Update

Thank you, Adam. At Riverwater Partners, we run concentrated portfolios and are long-term holders of companies with starting positions in the range of \$250 million to \$5 billion market cap companies. We stay roughly within 5% of sector weighting compared to the benchmark, but can go up to 10%.

Our top five holdings highlight idiosyncratic investments that we believe can perform well in volatile markets and hit on themes we are bullish on: energy, AI, and volatility. Our top five holdings are names you might not have heard about or heard on TV, but benefit from our bullish themes.

Our new top holding, Adeia, is a good example of an under-the-radar stock that benefits from the AI theme. Not only have they executed well, but they've also run up with other technology stocks. Adeia is a unique and undervalued way to play data center expansion. Adeia licenses intellectual property to customers for use in their media and semiconductor products and services. The growing and more exciting semiconductor segment's hybrid bonding technology is being used for the most complex chips going into data centers. We look for more partnerships to be announced in 2026 from this segment.

StoneX is a core holding in the portfolio because of its ability to not only compound earnings over time, but also its defensive characteristics when markets are volatile. As an investor, if you think volatility, uncertainty is here to stay, StoneX is a good place to be. Their first quarter earnings report was very strong, highlighting the earnings power these types of companies have in volatile markets like the ones we're currently in.

Kodiak Gas Services is an energy play. It's a compression company and now also a power play in the natural gas industry. Kodiak is founder-led and enables oil and gas companies to produce, gather, and transport natural gas. This is a play on natural gas volumes, electrification, LNG exports, and domestic demand. It's not a play on commodity prices as we think the secular theme for volumes will continue to grow over time. They're a top three player in compression with large cap customers with long-term contracts. And in early '26, they made a transformative acquisition when they acquired the distributed power systems that helps power manufacturing, microgrids, and data centers.

Also, Modine has also made it back into our top five, a name we have highlighted in the past. They benefited from data center build-out. The stock has done well year to date as hyperscalers have guided to further CapEx spend into 2027, and is a good example of a picks and shovels way to play the AI theme.

Now, we'll move to the sector weightings. In the small cap portfolio, we focus on stock selection over sector weighting, but have sectors we like more than others. Maybe one of the major changes we had from our last webinar was we went from being pretty bullish on consumer discretionary to underweight on consumer discretionary. Many of the benefits we saw coming into this year were upended by the war in the Middle East. Those examples were higher tax refunds, easing tariff pressure, falling interest rates, and potentially deferred consumer spending that was being shifted into 2026. Well, a lot of those have now been delayed, even though higher tax refunds have come through. They've been eaten up by energy and higher gas prices.

So we currently have a small position in Warby Parker, which is more of a benefit of AI glasses, and Grand Canyon University, which we view as more of a stable company. When you look at this slide, you might see that consumer discretionary actually is an overweight. That's because as of last quarter, Atmos was categorized as consumer discretionary. It has since finally been reclassified as industrial. So, as of today, we are underweight even though that slide might not show that.

We still like industrials that are tied to AI infrastructure, manufacturing activity, and domestic investment. Good example of this is NPK International, Performance Line Products, and again, Modine. Our large underweight in healthcare is driven by not only biotech companies, which make up roughly 50% of the Russell 2000 healthcare sector.

In the last quarter, we were able to find a real estate name, Cushman Wakefield, that was sold off during the AI scare. And we believe the price action was overdone to the downside, so we did add that name, and we did do a deeper dive write-up in our first quarterly letter, which is available on our website if you'd like to learn more about that company.

So overall, in '26, I think it's become more risky as this Middle Eastern war lingers on. We have used that volatility to add quality names, and hopefully we get opportunities to add more.

Moving to portfolio characteristics. As you can see, we focus on higher quality names that have better returns on equity and returns on invested capital. We are willing to pay more for some great companies if we think valuation is still reasonable. An interesting fact, unprofitable companies are excluded from the benchmark statistics, and if they were added back, would increase the valuation numbers of the benchmark.

All right. And moving to performance. So the small cap portfolio outperformed the Russell 2000 in the first quarter, the nice bounce back from 2025. We did have two buyouts in the last quarter. That was SunOpta and Talkspace, which helped performance.

So yeah, if you look on the right side, financials was our largest detractor. So it's driven by Coastal Financial. Coastal experienced a little bit more of a volatile quarter with the stock performance shaped by the evolving investor perception around the risks tied to their FinTech partner ecosystem, and also some of the private credit dynamics that were circulating in the first quarter. So investors grew a little bit more wary of that relationship and ended up hurting the stock. Fortunately, we did reduce our position in the early beginning of the first quarter. So it is a lower weighting now, so you'll see that it's out of the top five. But we still do think their core business is solid.

On the left side, you'll see our top performing sector was information technology. Stock selection within the sector was the primary driver of the strong positive attribution as several of our technology holdings delivered double-digit returns. This was driven by the resurgence in semiconductor investment thesis and continued CapEx spend by the hyperscalers. You see

Modine was the top performer, and we mentioned that earlier.

So moving to the trailing one-year returns. Yeah, we have still underperformed for the trailing one year. Our strategy will usually underperform in more speculative rallies like we had in the second half of '25, and that was driven again by biotech, high short interest stocks, and unprofitable companies. And you can see that reflected on the right side of the slide there, where healthcare was our biggest detractor for those same reasons.

And then if you look on the left side, our top sector was materials, and that was driven by Uranium Energy Corp and Centrus. However, we have exited both of those positions. While we're still bullish on the nuclear and uranium space, both those names kind of got tied into the AI trade, and their valuations became a little disconnected from the reality of where uranium prices were. And also, our thesis kind of played out for Centrus as they finally received DOE funding, and the stock reflected that, and now kind of the hard part of actually building out that enrichment is probably going to be a little bit more difficult. So if valuation was correct, I could see us re-entering that industry.

Yeah, the small cap strategy is presented here relative to its benchmark, the Russell 2000. As a reminder, in compliance with SEC's marketing rule, all performance data presented today reflects net of fee returns based on the highest fee schedule applicable to retail clients, which is 1%.

ADAM PECK — Sustainable Value Strategy

And I'll pass it back to Adam. Great. Sorry. Muted there. Thank you, Nathan. I think Nathan had a really hot hand in the first quarter, and I think was touching his computer, which caught fire, so he's sharing computers with Matt for the rest of the webinar.

But, happy to walk through the sustainable value strategy. So, from a portfolio concentration perspective, very similar to what Nathan described. But we just want to make it known, we've been very intentional when constructing portfolios. So concentrated, it's because we only invest in our best ideas. Sector weight guardrails to ensure that our alpha is driven by stock selection over the long term. And we take a long-term approach, with turnover less than 35%, thinking in years, not in quarters and days.

So, top five for sustainable value. Our long-term view, I think, is really evident in the top five, because two of the five have been in the strategy since day one, which is Quest and Grand Canyon Education. We've only owned Everest since 2024, when it was spun off from another holding, which we bought before MDU. We've owned EZZ for a number of years.

But getting back to Everest at the bottom, it's headquartered in Bismarck, North Dakota, provides electrical, mechanical contracting, as well as transmission and distribution services.

Electrical and mechanical handles electrical communication, wiring, fire suppression for large buildings, and transmission distribution builds and maintains overhead, underground electrical gas and communications infrastructure for data center customers, chip manufacturers, and other high-tech end markets. And so this is what's driven it into a top five holding. And so it has been a top performer because of the AI trade.

From a sector weight perspective, no major changes, and no intentional bets. No sector differential here is more than 5%. Our two largest overweights are staples and healthcare. Two largest underweights, financials and communication services.

On the valuation, we've got slightly higher valuation metrics. Nathan did reference non-earners don't show up here. If you just took all the non-earners and gave them a multiple of 30 times earnings or whatever you thought was appropriate, 50 or 60, I think we would look much cheaper. But also, we have returns on capital that are about double the benchmark. And so higher return on capital companies do deserve better multiples, and obviously, growth is a component there. But there's definitely been a historically positive correlation between return on invested capital and valuation.

So onto performance. We did underperform in the first quarter on a relative basis by about 3%. When you look at the reasons for that, healthcare topped the list. Haemonetics was a top detractor in the first quarter. Funny enough, it was the best performer in the fourth quarter last year, and before that, it was the worst performer in the third quarter of last year. So the stock is multiples more volatile than their underlying business because their underlying business is selling equipment and disposable services to blood and plasma collection centers, which is very, very stable. They also have a vascular surgical market business.

And the stock has required patience, which a lot of investors are short on, but their position in the plasma market has seen strength with growing collection volumes and share gains, unfavorable pricing. And while the vascular surgical market has had some growing pains, we think it's on the mend. And so they've been investing in commercial teams and starting to see positive things on the horizon. We feel confident that they're going to be able to compete well fundamentally, and hopefully the market in the future are going to give them credit. It trades for 10.9 times next year's earnings, has a double-digit free cash flow yield. So, we're happy sticking around, being patient to see the market realize the success we think they'll have.

And then on the positive side, Plexus is a contract manufacturer. I believe I've talked about it in quarters here before. But then they had very good quarter, good guidance, and not surprisingly, they're levered to semi-cap equipment and robotics driven by AI. So they had a good quarter.

On the one-year numbers, last year's underperformance is being anniversaried by Liquidation Day, when low quality really took the forefront. So while we had double-digit absolute returns, we clearly have not kept up with the low-quality rally. Historically, low-quality rallies start to peter out about after 12 months, so I think we're getting close, but we have had fabulous winners.

I referenced us lightening up on the AI trade, and first and foremost would be Ciena. Ciena, I think we've owned since 2017. Maybe we bought it in 2018. Cindy can correct me when she hops on. But we've owned it for a while, and from about a year ago, it's been a 10-bagger. So when we owned it, it was sub \$10 billion. Today, I think it's an 80-something billion dollar market value. So we're now out of it, and we parted ways with the last of our holdings in the first quarter.

So like I said earlier, AI's been driving the market and our portfolios, but we have, on a net basis, been lightening up. And then on the right-hand side are our worst performers. We still own Tecnoglass and Limoneira, and we've owned them for a number of years, but we did part ways with Lantheus.

So last slide here, just on performance. Again, recent relative performance has trailed with low quality in '25, but we're very proud of our medium and long-term returns. And so with that, I will hand it over to Cindy.

CINDY BOHLEN — 2025 Sustainability Report

Great. Thanks, Adam, and thanks, everyone, for joining us today. I'm going to introduce Riverwater's 2025 Sustainability Report, which is available on our website. And this year's report explores Riverwater's responsible investing approach through the lens of two concepts of power, hence the title, "The Power of Responsible Investing." And the first one is the ability to act or produce an effect, and this looks at the power of Riverwater's responsible investing approach to create value. And the second is a source or means of supplying energy, which looks at our climate change scenario analysis as it relates to electric power generation. And the majority of my slides are actual pages from the report.

So starting on this slide, at Riverwater, we understand well that when applied responsibly, power can fuel value creation. And this graphic shows the 2025 Sustainability Value Triangle survey results, which conclude that sustainability should be understood as an important creator of business value — it's not simply a matter of cost reduction or compliance, but is best understood and practiced as a strategic driver that fuels growth, innovation, resilience, and trust. And we opened with this in our report because this is exactly how we view the role of responsible investing.

So turning to the power of our responsible investment framework, pillar one is due diligence, and this is the power of digging deep, where we seek to understand how portfolio companies steward their human, physical, and financial capital to conduct their businesses and generate returns. And as a reminder, our proprietary scoring system, which is pictured here, measures both a company's footprint, which is the impact of its operations on the environment and people, and also its handprint, the value brought to society by its actual products and services.

So the donut chart on the next page shows the footprint of the sustainable value strategy companies during 2025. And you can see a lot of the circles, the donuts, are completed here, and that's because virtually all of our companies have formal sustainability reporting and embrace diverse perspectives and alignment at the executive and board level. And likewise, our portfolio companies generally protect their workers, supply chains, and the communities in which they operate. The majority of our companies also give attention to physical factors, which is the middle row, like energy, water, and waste stewardship. And that is impressive because many of our companies have a very small environmental footprint because they're providers of services.

So the next page shows the handprint of the sustainable value strategy companies. And this is again how their business by its very nature brings a specific value to society as measured by the SDGs. And so we have a few companies that are bringing better health outcomes to the world, SDG 3. We have one working for better education, which is SDG 4, and we have quite a few that are bringing innovation, which is SDG number 9. And our report highlights several of the companies whose businesses are bringing these positive impacts to the world.

So the next two slides, which we'll just stop on briefly, are the same portrayal of the small cap strategies, footprint and handprint, and the results are very similar.

So turning to the next slide, which is our second pillar of engagement, which gives us the power of a seat at the table. As shareholders, we are in a good position to offer advice to our portfolio companies on how to improve their policy and practice as it relates to responsible business. Often, we help them begin the sustainability journey by suggesting a materiality assessment and by offering best practices for policy and reporting. And this graph indicates the SDGs which our engagement practice targeted during 2025.

And finally, our third pillar of collaboration is the power of partnership. We can't do this work alone. We rely on the organizations shown here to inform our practice and to sometimes power an engagement.

Turning to the concept of power as a means to supply energy, Adam and Nate have talked a lot about energy, and that's because 2025 witnessed a power debate surrounding AI, and that was the question of will the power of the promise of AI to solve the world's problems justify the cost to power AI? And really, the simple answer is we don't know, but what we do know is that the AI train has firmly left the station. And fortunately, we have found a lot of companies who are working to steer it in the right direction.

And so this page shows a lot of the information describing this electric power supply/demand dynamic, emanating from AI proliferation and why this question is so important today.

So on the next page, our report explored this topic and highlighted our first climate change

scenario analysis. We featured companies in our report that are well-positioned by virtue of the innovation they're bringing to help their customers reduce their greenhouse gas emissions. And we also did a deep dive of our utilities companies using our TCFD-aligned framework to assess risk and opportunity under the four scenarios pictured here.

And our work to help utility companies stay the course to add renewable power and to protect their assets from the effects of climate change is an example of how our attention to both the footprint and handprint brings value to our portfolios. And likewise, our investment in companies using innovation to bring real-world solutions to this problem demonstrates our belief in the power of the handprint to generate superior financial returns. And these aren't mutually exclusive outcomes, rather they are mutually reinforcing.

So again, our report can be accessed on our website, and thank you for your attention. Back to you, Matt.

MATT DRVARIC — Q&A

Thank you, Cindy. Thank you, Adam and Nate, for your updates on the Riverwater strategies and initiatives. At this time, we'll open the floor for any questions.

We did have one question that has come up in a lot of conversation over the past quarter, and Adam, I'll let you take this one, but you talk about tweaks made in the portfolio around the Iranian conflict. Can you elaborate on what has been done to better position the portfolios going forward over the next 12 to 18 months as we work through this time?

ADAM PECK — Q&A Response

Sure. Thanks, Matt. Yeah, March was a crazy time trying to figure out what the future was going to look like. And a lot of it hinges on what happens with the opening of the Gulf. So, none of us are smart enough to know really what the near term or medium term holds from a geopolitical standpoint. So we didn't make any wholesale changes in the portfolios.

Clearly, energy prices have all spiked, and that's filtering through the economy, and as Nate referenced, it did change our outlook. It had an impact on our outlook for the consumer. I hear a lot of people complaining about gas prices, and I believe that will impact how they go about their daily lives.

So the way we viewed it is we can't handicap the price of oil or price of natural gas, but as we looked at the destruction of supply coming out of the Middle East, we saw that, as an example, aluminum — about 9% of global aluminum comes out of the Middle East. And when the power goes out at an aluminum smelter, and if there's any aluminum basically in the pot lines, and

essentially it freezes by cooling down, and destroys the pot lines. So we think it'll be a number of years before aluminum supply globally can get back to where it was at the end of February or mid-March.

And so as we looked at the aluminum market in the US, it's crazy. We put this in our quarterly letter. If you go back to 1980, I believe there was about 30 aluminum smelters in the US. As of now, there's four. So production is down 90-plus percent in the US. The US had 33% of the global market share in 1980. Today, it's less than 2%. So everyone still uses a lot of aluminum in the US for cans and housing and automobiles. But we've outsourced it. And so now we're in a world where it's important to have secure supply that can't be bombed out.

So we think there's a long runway to supply in the US increasing. And the company that we bought trades at a single-digit multiple with earnings trajectories, we think, going up for a number of years. Will there be volatility in the stock? Yes, volatility quarter to quarter, but we think that's a long runway that we can underwrite versus trying to figure out what the price of oil is going to do in the short term. So that's just one way. We did make some tweaks on the edges. So where we see opportunity that we can benefit from over the long term, we will take it. And so hopefully that answered the question.

MATT DRVARIC — Closing

Thank you, Adam. That concludes the questions for today's call. As we wrap up, I reiterate our passion for small cap responsible investing. We believe this approach enhances opportunity by promoting resilience, capturing inefficiencies, and improving long-term return potential. We appreciate your time today and continued interest in Riverwater. If you have additional questions and would like to speak with a member of the team, please feel free to reach out to me. We look forward to talking with you again next quarter.