RIVERWATER PARTNERS

Transcript: Q2 2026 Riverwater Small Cap Strategies Webinar

00:00:55.830 --> 00:01:03.450
Matt Drvaric: Good afternoon to the east, and good morning to the west. Thank you for joining us today. We will begin momentarily.
00:01:11.650 --> 00:01:28.920
Matt Drvaric: Welcome to Riverwater Partners Second 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 during the presentation, please use the questions box located at the bottom of your control panel.
00:01:29.040 --> 00:01:34.210
Matt Drvaric: Please note that today's call is being recorded, and a replay will be made available following the webinar.
00:01:34.450 --> 00:01:37.099
Matt Drvaric: Let's begin with an overview of today's agenda.
00:01:37.760 --> 00:01:49.469
Matt Drvaric: This afternoon, I'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.
00:01:50.050 --> 00:01:55.630
Matt Drvaric: Nate Fredrick, Portfolio Manager, will provide a performance update on our small cap strategy.
00:01:56.020 --> 00:02:06.570
Matt Drvaric: To close, Cindy Bohlen, our Director of Responsible Investing, will talk about our third pillar of responsible investing, collaboration, and how we work with companies around water stewardship.
00:02:06.720 --> 00:02:09.310
Matt Drvaric: After the presentation, we'll address any questions.
00:02:13.150 --> 00:02:25.619
Matt Drvaric: Riverwater offers 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.
00:02:29.130 --> 00:02:37.559
Matt Drvaric: Looking at the strategies. The Sustainable Value Strategy finished the quarter with about $140 million in total assets, including UMA delivered.
00:02:38.010 --> 00:02:46.889
Matt Drvaric: The small cap strategy ended the quarter with nearly $100 million in assets, inclusive of assets, from the Accuitas Small Cap ETF launched in February.
00:02:47.360 --> 00:03:05.839

Matt Drvaric: We have continued to gain momentum with mission-driven organizations and families. Our team is looking forward to attending and connecting with you at the Leadership Conference of Women Religious, the Catholic Faith Investor Summit, and the National Association of Securities Professionals Consultant Retreat in the coming months.

00:03:08.140 --> 00:03:11.190

Matt Drvaric: Following the end of the quarter, effective July 1st.

00:03:11.260 --> 00:03:18.270

Matt Drvaric: We are proud to name Nate Fredrick Co-Portfolio Manager, alongside Adam across all small cap strategies.

00:03:18.320 --> 00:03:31.709

Matt Drvaric: Nate has been with the firm since day one, starting as an intern while completing graduate school, and is a valuable member of the team who is passionate about investing. Congrats to you, Nate. Happy for you to see your success.

00:03:31.990 --> 00:03:45.769

Matt Drvaric: We remain energized by the opportunities ahead in both strategies. Our team is grateful for your continued consideration and the trust you place in us each day to deliver our mission to make the world a better place by growing wealth through responsible investing.

00:03:45.900 --> 00:03:51.459

Matt Drvaric: I'll turn it over to Adam, who will share commentary insight around the small cap market. Adam.

00:03:52.720 --> 00:04:10.060

Adam Peck: Thanks, Matt, and good day to everyone. I hope we all had a nice weekend. I'll cover, as Matt said, our sustainable value strategy, but before that, I'll walk through major themes driving the year-to-date market, namely high beta stock performance and memory, and that we had no memory.

00:04:10.230 --> 00:04:15.050

Adam Peck: That is exposure to memory stocks, not cerebral issues on our end.

00:04:15.820 --> 00:04:21.770

Adam Peck: I spoke to this in our last few webinars, but I think the points I'm gonna make, bear repeating again.

00:04:21.940 --> 00:04:35.680

Adam Peck: Given the magnitude and duration of the trend. The Russell 2000 had its best first 6 months since 1991. I'm thrilled to see small caps become relative performance leaders, as we've been waiting and waiting.

00:04:36.220 --> 00:04:55.929

Adam Peck: With that said, the manner in which small caps are compounding capital are not driven by factors we gravitate to. Namely, profitability with good returns on capital, solid balance sheets, and attractive valuations, all factors that inevitably result in owning lower beta stocks to the market.

00:04:56.410 --> 00:05:00.930

Adam Peck: High beta companies put in their best quarter in over 10 years.

00:05:01.440 --> 00:05:07.400

Adam Peck: The gains we saw were driven by loss-making companies, which beat profitable companies by over 12%,

00:05:07.670 --> 00:05:21.490
Adam Peck: And the S&P 600, which has a profitability requirement, is now on track to underperform the Russell 2000 for the third straight year, which is a first. I'll visually walk through all of these points in the next few slides.
00:05:22.940 --> 00:05:25.860
Adam Peck: So, Hive Beta has been the place to be.
00:05:26.090 --> 00:05:30.639
Adam Peck: This chart goes back 10 years, and is broken out by quarters.
00:05:30.790 --> 00:05:39.719
Adam Peck: In the 40 quarters shown here, you can see that high beta underperformed in more than half of all quarters on the right.
00:05:40.460 --> 00:05:46.320
Adam Peck: 25% of the time, high beta underperforms by more than 5% in a quarter.
00:05:47.240 --> 00:05:57.029
Adam Peck: In 9 of the quarters over on the left, it beat by… high beta beat by less than 5%, and in another 9 quarters, it beat by more than 5.
00:05:57.660 --> 00:06:03.289
Adam Peck: And High Beta's 3 best quarters have all come in the last 12 months.
00:06:03.710 --> 00:06:12.750
Adam Peck: This most recent quarter blows every other quarter out of the water by a large margin. Again, not a factor in our favor.
00:06:13.920 --> 00:06:20.510
Adam Peck: There's likely a high correlation between high-beta and loss-making companies.
00:06:20.970 --> 00:06:26.579
Adam Peck: The next chart shows profitable companies in the Russell 2000, in green.
00:06:26.710 --> 00:06:30.660
Adam Peck: Performance versus loss-making companies' performance in red.
00:06:31.530 --> 00:06:40.970
Adam Peck: It shows quarterly performance for each. Unprofitable companies in red have outperformed profitable in green for 4 of the last 5 quarters.
00:06:41.170 --> 00:06:45.550
Adam Peck: The cumulative outperformance has now hit over 31%.
00:06:45.820 --> 00:06:47.129
Adam Peck: Over the last 5.
00:06:47.590 --> 00:07:02.669
Adam Peck: And across both portfolios, we have only one stock that may be unprofitable in 2026. So, for sure, 98% of our holdings are profitable, and just… compares to just 60% for the Russell 2000.
00:07:04.810 --> 00:07:11.940
Adam Peck: This next chart shows the same data, exact same data, in a different form, to give it a historical look back.
00:07:12.210 --> 00:07:21.949

Adam Peck: That is, unprofitable companies' returns minus profitable companies. When the line is red, unprofitable companies are beating profitable.
00:07:22.170 --> 00:07:28.080
Adam Peck: The important point to make is that over the long term, profitability wins, as the green line
00:07:28.470 --> 00:07:32.170
Adam Peck: Is evident here in the chart the vast majority of the time.
00:07:33.020 --> 00:07:35.940
Adam Peck: I'm thinking it's well over two-thirds of the time.
00:07:36.150 --> 00:07:50.030
Adam Peck: But when unprofitable companies prevail, the magnitude can be severe, though it does revert back pretty quickly. So while there could be more pain to come, I would expect this trend to revert, given historical precedent.
00:07:51.650 --> 00:07:53.750
Adam Peck: And as I already mentioned.
00:07:53.930 --> 00:08:00.689
Adam Peck: The S&P 600 on the next slide is a good indicator for how quality companies are doing.
00:08:01.410 --> 00:08:11.569
Adam Peck: And right now, it's tracking for a record-breaking third year of underperformance to the Russell. The duration of this low-quality rally is getting very, very long in the tooth.
00:08:13.130 --> 00:08:17.090
Adam Peck: And then duration can be seen on the next chart again.
00:08:17.190 --> 00:08:24.809
Adam Peck: quality, which is measured by comparing the top two quintiles in the Russell 2000 to the rest of the index.
00:08:25.220 --> 00:08:38.339
Adam Peck: We are 5 quarters in, and the longest run previously to this was 6 quarters, coming out of the very short 5-week COVID bear market, which turned into the monster meme and SPAC rally.
00:08:41.150 --> 00:08:42.990
Adam Peck: So, to remind everyone.
00:08:43.260 --> 00:08:51.250
Adam Peck: On the next slide, we run focused portfolios targeting low turnover and strive to create alpha through stock selection.
00:08:51.550 --> 00:09:04.359
Adam Peck: When running focused, active portfolios, we have biases that are built into the portfolios. I think they're good biases. That is, investing in quality companies that make money and earn their cost of capital.
00:09:04.820 --> 00:09:12.830
Adam Peck: That have strong balance sheets and management teams, and we favor these factors because they've proven to outperform over the long term.
00:09:13.500 --> 00:09:15.889
Adam Peck: Sometimes these factors are out of style.

00:09:16.020 --> 00:09:17.150
Adam Peck: like now.
00:09:17.480 --> 00:09:26.619
Adam Peck: Times like these demand disciplined process to not chase story stocks with bad fundamentals, because as I've just shown, they eventually revert.
00:09:26.850 --> 00:09:35.330
Adam Peck: And so, with that all in mind, we continue to apply our philosophy and process with patience and in the context of careful risk management.
00:09:35.410 --> 00:09:50.849
Adam Peck: And as Matt mentioned, Nate's promotion to Copium was very well deserved. He's been on the team now for over 9 years, and has been a big contributor to the success we've had. So, with that, congrats to Nathan, and I'll pass it off to you.
00:09:53.110 --> 00:10:02.479
Nathan Fredrick: Thanks, Adam, and thanks for everyone for joining today. I'll be covering the second quarter for the small cap strategy.
00:10:02.760 --> 00:10:03.910
Nathan Fredrick: Next.
00:10:05.250 --> 00:10:22.510
Nathan Fredrick: So, yeah, just a quick reminder, we benchmarked to the Russell 2000, we purchase companies within the market cap of $250 million to $5 billion, and we also run a concentrated portfolio of between 30 to 45 names.
00:10:23.660 --> 00:10:33.080
Nathan Fredrick: And additionally, on this slide, we keep sector weights within 5 percentage points of the Russell 2000, with a hard limit up to 10.
00:10:34.060 --> 00:10:35.040
Nathan Fredrick: Next.
00:10:37.350 --> 00:10:50.369
Nathan Fredrick: So our top 5 holdings make up about 21% of the portfolio. I wanted to highlight two names in our top 5 that we haven't really highlighted in the past, and are now larger weights in the portfolio.
00:10:50.820 --> 00:10:59.590
Nathan Fredrick: I'm also calling out these two names that hit on the AI picks and shovels and grid electrification theme that has done well this year.
00:10:59.950 --> 00:11:06.359
Nathan Fredrick: The first one is Perform Line Products, which is now our largest position at 4.8%.
00:11:06.770 --> 00:11:16.869
Nathan Fredrick: Provides products and systems used in constructing and maintaining overhead and underground networks, mostly for the utility and telecommunications industry.
00:11:17.260 --> 00:11:22.460
Nathan Fredrick: Basically, most of their products you can see on large transmission lines across the country.
00:11:22.610 --> 00:11:28.630

Nathan Fredrick: It sits right in the middle of the grid and electrification build-out that the AI theme is now driving.
00:11:29.370 --> 00:11:37.640
Nathan Fredrick: And Digi International, at 4.4%, is our industrial Internet of Things connectivity holding.
00:11:37.920 --> 00:11:47.570
Nathan Fredrick: Digi was up about 55% in the quarter as demand for connected infrastructure accelerated alongside AI and automation.
00:11:47.780 --> 00:11:53.790
Nathan Fredrick: It grew into one of our largest positions, and we did trim it modestly to keep our sizing disciplined.
00:11:54.220 --> 00:12:02.200
Nathan Fredrick: Additional names here. StoneX, again, is in our top 5 that I'll discuss more in our performance slide.
00:12:02.310 --> 00:12:10.049
Nathan Fredrick: Kodiak, we have highlighted in the past that sits nicely in the part of the energy and AI investment theme.
00:12:10.490 --> 00:12:22.740
Nathan Fredrick: And I also want to draw your attention to PDF Solutions. We did a deeper dive into PDFS in our quarterly letter, if you'd like to learn more about an interesting company in the semiconductor space.
00:12:23.560 --> 00:12:32.900
Nathan Fredrick: So, moving on… So sector weightings, were meaningfully overweight industrials and information technology.
00:12:33.560 --> 00:12:38.909
Nathan Fredrick: That's where we're finding the highest quality small caps and some of the current themes we have been discussing.
00:12:39.390 --> 00:12:43.459
Nathan Fredrick: We're notably underweight healthcare and consumer discretionary.
00:12:43.890 --> 00:12:47.609
Nathan Fredrick: That healthcare underweight is deliberate and driven by biotech.
00:12:47.850 --> 00:12:56.420
Nathan Fredrick: However, we are looking to add to other parts of the healthcare industry, as performance of the whole sector has broadened recently outside of just biotech.
00:12:56.940 --> 00:13:03.789
Nathan Fredrick: But we became more bearish on the consumer as the Iran war started and oil and gas prices rose.
00:13:03.970 --> 00:13:17.509
Nathan Fredrick: We enter the current period less bearish on the consumer than we were 3 months ago, and could be a sector where we add, in the future, as the consumer has ended up being more resilient and energy prices have come down.
00:13:17.650 --> 00:13:22.920
Nathan Fredrick: We would consider buying either consumer discretionary or consumer staples.

00:13:23.440 --> 00:13:25.030
Nathan Fredrick: Next.
00:13:27.000 --> 00:13:38.570
Nathan Fredrick: Yeah, this slide, is our quality bias shown in the numbers. Our holdings earn a return on equity of about 14% versus under 2% for the Russell 2000.
00:13:38.780 --> 00:13:43.160
Nathan Fredrick: An enormous gap that reflects how much more profitable our businesses are.
00:13:43.320 --> 00:14:01.019
Nathan Fredrick: We also carry less leverage. Long-term debt-to-capital of 28% versus 37% for the index. We do pay modestly higher multiples for that quality, but we think stronger returns and cleaner balance sheets are worth it, particularly late in the cycle.
00:14:02.520 --> 00:14:03.660
Nathan Fredrick: Next.
00:14:05.200 --> 00:14:09.210
Nathan Fredrick: Alright, this slide is, last quarter's performance.
00:14:09.570 --> 00:14:28.420
Nathan Fredrick: The quarter itself was defined by two forces pulling the same way, an accelerating AI build-out and a geopolitical oil and gas supply shock that became resolved, then was back on, then resolved again, and depending on the time, it could be resolved or on again.
00:14:28.430 --> 00:14:39.599
Nathan Fredrick: What this led to was, one of the most powerful risk-on quarters for small caps in recent memory, with the Russell 2000 up more than 21%.
00:14:40.150 --> 00:14:48.870
Nathan Fredrick: It was also, like Adam said, distinctly lower quality, higher beta rally, exactly the kind of environment that tests a quality process like ours.
00:14:49.290 --> 00:14:58.400
Nathan Fredrick: We did… we participated meaningfully, but did end up trailing. As you can see in the top right, our total active return was negative 2.5%.
00:14:58.950 --> 00:15:10.970
Nathan Fredrick: Right below that, you'll see our energy overweight added 105 basis points, driven by our tilt towards gas compression and services, rather than the commodity producers.
00:15:11.100 --> 00:15:21.729
Nathan Fredrick: the energy sector was actually negative for the quarter, even with the supply shock. Well, we were… we ended up positive. This was driven by Kodiak, which we mentioned earlier.
00:15:22.380 --> 00:15:38.650
Nathan Fredrick: On the left side, you'll see our top contributor was StoneX, and contributed 274 basis points. The Middle East volatility drove exceptional trading and clearing activity, leading to shares up… being up 47%.
00:15:38.680 --> 00:15:50.200
Nathan Fredrick: We did trim into the strength, as volatility can be mean-reverting, and it would be difficult to reproduce such great earnings in the future. But like you saw, it's still one of our top 5 holdings.
00:15:50.590 --> 00:16:01.079

Nathan Fredrick: On the lower right, the detractors, you'll see was healthcare. Our biggest sector drag at negative 357 basis points.
00:16:01.080 --> 00:16:13.030
Nathan Fredrick: They basically came from being underweight, a healthcare sector that surged in the quarter, led by speculative pre-revenue biotechs. We don't own pre-revenue biotech as a matter of our process.
00:16:13.800 --> 00:16:24.840
Nathan Fredrick: Looking at the detractors on the left, our profitable healthcare names like LaMate, and our largest single detractor, Grand Canyon Education, were simply left behind in a market that rewarded beta.
00:16:25.080 --> 00:16:32.809
Nathan Fredrick: The investment theses are still intact, but it's difficult for these types of names to outperform in a speculative market.
00:16:33.740 --> 00:16:34.850
Nathan Fredrick: Next.
00:16:36.800 --> 00:16:45.689
Nathan Fredrick: So if you zoom out to a year, you see a similar pattern. Looking again at the top right, total active return was negative 9.4.
00:16:45.930 --> 00:17:03.089
Nathan Fredrick: Below that, information technology was our top contributory sector, which added 605 basis points over the past year. This was driven by our semiconductor exposure and IP companies like Audia that you see on the left as a top contributor.
00:17:03.440 --> 00:17:12.489
Nathan Fredrick: And then our number one contributor was Modine, a thermal management business that's been a direct beneficiary of data center cooling demand.
00:17:12.650 --> 00:17:17.360
Nathan Fredrick: We have since sold Modine, as we believe it has become fairly valued.
00:17:18.240 --> 00:17:32.759
Nathan Fredrick: On the lower right, again, you'll see healthcare allocation was the largest drag on the portfolio. As you spoke about previously, speculative biotech was a large outperformer over the last year, while higher quality med tech was an underperformer.
00:17:32.940 --> 00:17:46.549
Nathan Fredrick: On the left side, you'll see our top detractor was Technoglass, which is our multi-family commercial and single-family glass company. Cost us 202 basis points.
00:17:47.140 --> 00:17:55.270
Nathan Fredrick: As construction and markets softened, and the long-end interest rates have risen, dampening the single-family housing sector.
00:17:55.380 --> 00:18:05.549
Nathan Fredrick: This weighed on sentiment for the stock price, but we still believe Technoglass has a better business model than its peers, and will come out of this downturn in a stronger position.
00:18:06.810 --> 00:18:07.730
Nathan Fredrick: Next.
00:18:08.800 --> 00:18:18.999

Nathan Fredrick: So where does this leave us? For the quarter, we were up, but slightly trailed a large move in our benchmark. However, as of today, year-to-date, we are still outperforming.
00:18:19.150 --> 00:18:25.819
Nathan Fredrick: Also, I wanted to highlight, as of the end of July, the small cap strategy will now be 4 years old.
00:18:26.410 --> 00:18:41.350
Nathan Fredrick: In bringing it back to Adam's comments earlier, quarters like this one test the patience that quality investing requires. Our process of owning superior businesses with superior management at reasonable valuations doesn't bend to a single quarter.
00:18:41.350 --> 00:18:49.590
Nathan Fredrick: And we believe that consistency is exactly what serves this portfolio when speculative Leadership inevitably narrows.
00:18:49.690 --> 00:18:52.409
Nathan Fredrick: So now I'll pass it on to Adam.
00:18:54.530 --> 00:18:55.520
Adam Peck: Thanks, Nathan.
00:18:57.050 --> 00:19:02.210
Adam Peck: So again, I'll cover the sustainable, value strategy.
00:19:02.760 --> 00:19:07.229
Adam Peck: We run a focused portfolio, we try to keep within…
00:19:07.410 --> 00:19:19.259
Adam Peck: plus or minus 5% of our benchmark with hard limits at 10. We try to think long-term, and historically have, thinking about owning stocks for years, not quarters or months.
00:19:19.440 --> 00:19:27.389
Adam Peck: And we… Hone in on companies with, initially, between market caps of $500 million and $15 billion.
00:19:30.720 --> 00:19:42.639
Adam Peck: So, on to the next slide. We've got our top 5, for the strategy. All the top 5 have grown to be here, as average position size, is normally about 3%.
00:19:42.740 --> 00:19:54.230
Adam Peck: I'll mention AZZ as our top holding, which we've owned for over 5 years. It's a very good example of an ideal river water holding. It's a superior business.
00:19:54.230 --> 00:20:13.570
Adam Peck: It's got two segments, galvanizing and pre-coat metals. Galvanizing protects steel from corrosion, and pre-coat, for lack of a better term, coats metals, like steel and aluminum, for customers across many markets, including appliances, like refrigerators and washers, garage doors, and metal cans.
00:20:13.890 --> 00:20:26.289
Adam Peck: It's a great business, because galvanizing is a very local process, as it gets very expensive to move and transport large steel objects. Think transmission line towers.
00:20:26.530 --> 00:20:41.869
Adam Peck: So, they end up with very defensible businesses with great margins and returns on capital. AZZ has double-digit operating margins, a 10% free cash flow margin as well, and a 20% return on equity over the last year.

00:20:42.410 --> 00:20:48.579
Adam Peck: Growth has been driven by the construction of data centers, the electrical grid, bridges, and highways.
00:20:48.700 --> 00:20:57.310
Adam Peck: AZZ should benefit from secular trends in infrastructure, renewables, reshoring, and the transition from plastics to aluminum.
00:20:57.990 --> 00:21:06.089
Adam Peck: It has a solid management team. I've been following the company for probably close to 20 years, and I've always been impressed with their capital decision making.
00:21:06.200 --> 00:21:24.820
Adam Peck: The stock is no longer a deep value after the strong performance of the last couple years. It trades attractively to the market with much better returns on capital and a clean balance sheet. Plus, we think there's an opportunity to cash in on a 40% ownership of a JV, which was an old business that they sold.
00:21:24.840 --> 00:21:33.470
Adam Peck: And we think that, business could be sold within the next 12 months. It could generate a 9-figure inflow of cash.
00:21:34.090 --> 00:21:43.449
Adam Peck: So for the sake of time, I'm not going to delve into each of the other four names in as much detail as I just did for AZC.
00:21:43.680 --> 00:21:58.620
Adam Peck: Audia, Plexus, and NETSCOUT are all IT names, and Quest Diagnostics is a long-term healthcare name that we've owned since day one, so we've almost had that in the portfolios for 10 years.
00:21:58.780 --> 00:22:06.730
Adam Peck: So I'll say that each of these meet our three pillars of superior business, strong management, and attractive valuations.
00:22:08.820 --> 00:22:17.849
Adam Peck: Moving over to our sector weightings, I'll remind everyone we, like, again, we stay… try to stay within 5% on Fast and Harlem at 10.
00:22:18.150 --> 00:22:27.919
Adam Peck: It was a crazy end to the quarter. The Russell rebalance happened a little later than normal, and it happened, like, a day or two before the quarter ended.
00:22:28.770 --> 00:22:34.020
Adam Peck: So with the Russell Rebounds, the IT weight dropped from the high teens.
00:22:34.370 --> 00:22:37.380
Adam Peck: On average, over the quarter, to just 10%.
00:22:38.740 --> 00:22:45.660
Adam Peck: So, large-cap tech stocks that were in our benchmark, like SanDisk, moved over to the Russell 1000.
00:22:46.100 --> 00:22:52.750
Adam Peck: Over the average of the quarter, we had a slight underweight to tech at just under 17%.
00:22:53.830 --> 00:23:01.010

Adam Peck: But… The current, 7.4%
00:23:01.140 --> 00:23:04.580
Adam Peck: waiting of IT, because it… because it dropped.
00:23:04.690 --> 00:23:13.190
Adam Peck: I'm sorry, the current 10% weighting causes us to have about an immediate 7.5% overweight, which wasn't intentional.
00:23:13.350 --> 00:23:29.000
Adam Peck: So we like the tech names we own, but now, given the chance, we probably won't be adding additionally to tech names. And on the flip side, we'll probably be looking, and have at least over the last month, taking our tech weighting down slightly.
00:23:30.250 --> 00:23:51.289
Adam Peck: So, on the next slide, if you've been following us for a while, you see not much has changed here. We are a smidge higher on valuation, with our forward P.E. at about 15.6 versus 14.5, but like Nate said, sustainable value has the same quality metrics, much higher returns on equity.
00:23:51.330 --> 00:23:56.590
Adam Peck: Lower debt-to-cap, you can see a lower beta since inception.
00:23:57.290 --> 00:24:12.370
Adam Peck: So, and the sustainable value doesn't have any money-losing companies, whereas our benchmark has, quite a big number. I expect every company to be profitable, this year, so, again,
00:24:12.570 --> 00:24:21.509
Adam Peck: Just want everyone to take home, while our valuation's slightly higher, it is, a much higher quality, portfolio compared to the benchmark.
00:24:22.880 --> 00:24:28.309
Adam Peck: So, on to the craziness of the end of the year, really.
00:24:28.580 --> 00:24:39.069
Adam Peck: I didn't check, but I'm pretty certain a record was broken in the Russell 2500 value, with one stock contributing over 6% to a 12-month return.
00:24:39.500 --> 00:24:46.030
Adam Peck: And that stock was SanDisk, which was spun out of Western Digital in the middle of 2025.
00:24:46.160 --> 00:24:50.770
Adam Peck: It began this year, 2026, with a market cap above $40 billion.
00:24:51.590 --> 00:24:56.959
Adam Peck: It ended this last quarter with a market cap over $250 billion.
00:24:57.310 --> 00:25:08.969
Adam Peck: We focus on buying companies with market caps, as I said before, below $15 billion. So, even at the beginning of this year, this stock was not a candidate for addition to the portfolio.
00:25:09.330 --> 00:25:13.780
Adam Peck: And it was responsible for a majority of our relative underperformance.
00:25:13.950 --> 00:25:21.069

Adam Peck: Unfortunately for us, SanDisk was kicked out of the Russell 2500 value right at the end of the quarter.
00:25:21.960 --> 00:25:25.040
Adam Peck: And in this quarter to date.
00:25:25.180 --> 00:25:43.069
Adam Peck: it's… it's down a lot. It ended up, and I just saw this over the weekend, it ended up being the worst performing stock in the S&P 500 in July. I think it was down 47%. But we can't get back any of that relative performance, because it's now gone from our small cap index.
00:25:44.270 --> 00:25:48.519
Adam Peck: So with that, as I set up to, attribution.
00:25:48.740 --> 00:25:55.229
Adam Peck: You can see here, all of our underperformance was due to stock selection.
00:25:55.320 --> 00:26:06.279
Adam Peck: It was an outstanding quarter on an absolute basis. As you'll see in a few slides, we were up over 14%. We just didn't have enough beta, and as I already mentioned, missed out on Sandis.
00:26:06.370 --> 00:26:15.339
Adam Peck: The funny thing here is that our two top contributors, Vico and Plexus, are both tech stocks, but our largest sector detractor was tech.
00:26:15.730 --> 00:26:25.279
Adam Peck: This dichotomy is because our tech names were up only 50%, while the benchmark was up 75%. Again, this is in one quarter.
00:26:25.660 --> 00:26:35.720
Adam Peck: So we clearly have had great stock picks from Cindy in tech, with exposure across a number of AI-related names, we just didn't own the large caps, and…
00:26:35.850 --> 00:26:37.160
Adam Peck: That was intentional.
00:26:39.010 --> 00:26:48.009
Adam Peck: Same thing on, the one-year return. It's much more of the same. SanDisk is responsible for about a third of our underperformance.
00:26:48.120 --> 00:26:57.440
Adam Peck: And as I mentioned, low quality is responsible for another large chunk, and then I think biotech was a decent contributor to our healthcare underperformance.
00:26:59.720 --> 00:27:10.520
Adam Peck: So, again, I… based on the slides I showed everyone at the beginning, I believe we are getting into the very late innings and hopefully not expecting a doubleheader.
00:27:11.460 --> 00:27:30.080
Adam Peck: For absolute returns, on the next slide, as I said before, fantastic. Near-term absolute results. If we could compound capital at over 14% a quarter, everyone would be very happy. I don't expect that to be the case, but as we just discussed, we're underperforming on a relative basis.
00:27:30.200 --> 00:27:44.929
Adam Peck: I'm excited for the next quarter, when we'll be able to add a 10-year column to this slide, which will exactly match the since-inception column. And with that, I pass it over to Cindy.

00:27:46.220 --> 00:28:03.900
Cindy Bohlen: Thank you, Adam, and thanks to everyone for joining us. So today, I'm going to talk about collaboration, which is the third pillar of Riverwater's responsible investment practice. As a reminder, our three pillars are due diligence, engagement, and collaboration.
00:28:04.360 --> 00:28:23.309
Cindy Bohlen: collaboration with thought leaders informs us about environmental and social issues so that we can effectively offer insight to our portfolio companies and other stakeholders. And today, I'm going to talk about our collaboration efforts related to water stewardship.
00:28:24.020 --> 00:28:33.460
Cindy Bohlen: In April of this year, Riverwater convened a panel at the B Corp 2026 Champions Retreat, which was held in Milwaukee.
00:28:33.630 --> 00:28:42.339
Cindy Bohlen: Our panel, Water as a Force for Good, was an exploration of how individuals and businesses
00:28:42.410 --> 00:28:55.660
Cindy Bohlen: Working in partnership or in collaboration with investors and policy makers can turn small ripples of impact into waves of systemic change.
00:28:56.140 --> 00:29:07.810
Cindy Bohlen: And our dialogue left the audience with several important conclusions about water stewardship as a tenet of responsible… of responsible business practice.
00:29:08.530 --> 00:29:16.520
Cindy Bohlen: So on the next slide, you can see Karen Frost, President of the Water Council, which is one of our very strong
00:29:16.640 --> 00:29:31.459
Cindy Bohlen: collaboration partners, described how its WAVE water stewardship program helped a multinational company discover the reason for one of its location's outlier water use and expense.
00:29:31.560 --> 00:29:37.499
Cindy Bohlen: It was that the location's water supplier was stealing much of its water.
00:29:37.640 --> 00:29:46.930
Cindy Bohlen: But this is a great example of how the power of digging deep can preserve both water and profitability.
00:29:47.500 --> 00:30:01.690
Cindy Bohlen: Likewise, Amy Taylor, CEO of Zevia, which is a good-for-you soda, talked about how she asked her CFO to make a report detailing the cost savings from a change in their manufacturing process.
00:30:01.790 --> 00:30:12.319
Cindy Bohlen: She also asked him to report on the change in water and energy use. Unsurprisingly, the manufacturing changes not only reduced costs.
00:30:12.470 --> 00:30:23.720
Cindy Bohlen: but also water and energy consumption. And this is a great example of how responsible often equals profitable in business.
00:30:24.640 --> 00:30:41.470

Cindy Bohlen: Joel Bromier, president of the Alliance for the Great Lakes, shared a story of a chemical company's science discovering that a particular chemical used in one of its products wasn't necessary to get the desired results.
00:30:41.880 --> 00:30:54.629
Cindy Bohlen: They removed the chemical, and then reported the findings to policymakers, which resulted in the chemical ultimately being banned. And so this is a great example of collaboration
00:30:54.770 --> 00:30:59.850
Cindy Bohlen: Using market dynamism first to lead policy.
00:31:00.330 --> 00:31:15.650
Cindy Bohlen: And finally, Wisconsin State Senator Jody Habish-Siniken encouraged business leaders to invite policy makers to work with them to help balance environmental and social outcomes.
00:31:15.700 --> 00:31:22.870
Cindy Bohlen: with financial outcomes. And that's exactly what our practice seeks to do with collaboration.
00:31:23.830 --> 00:31:37.000
Cindy Bohlen: So the next slide highlights our collaboration partners relating to water stewardship. CERES convenes investor coalitions on water and climate risk. We have been part of their valuing
00:31:37.000 --> 00:31:48.000
Cindy Bohlen: Water Finance Initiative. The Water Council, which I've highlighted here, offers its WAVE program for corporate water risk analysis and stewardship.
00:31:48.120 --> 00:32:05.899
Cindy Bohlen: And CDP coordinates global water security disclosure data. And our collaboration with these experts promotes this sharing of ideas that I'm talking about in working in partnership towards stewarding our shared systems like water.
00:32:06.590 --> 00:32:13.160
Cindy Bohlen: And so finally, looking at a couple of examples of river waters informed water stewardship.
00:32:13.340 --> 00:32:21.490
Cindy Bohlen: At the time of purchase, Riverwater engaged Limanera, which is a lemon and avocado grower on water stewardship.
00:32:21.860 --> 00:32:41.200
Cindy Bohlen: And Limanero, over time, has worked to improve its water footprint by converting 87% of its irrigation systems to drip and microsprinkler. And these systems use, on average, like, 2.5 acre-feet per acre of water, respectively.
00:32:41.200 --> 00:32:58.709
Cindy Bohlen: Compared to 13.8 for flood irrigation. And this is very important work because agriculture accounts for about 70% of global freshwater withdrawals. This helps protect that shared resource that we have.
00:32:59.120 --> 00:33:18.080

Cindy Bohlen: And likewise, at the time of purchase, we engaged with Vico. Vico is a maker of the equipment that makes semiconductors, or computer chips. And we had a talk with them about their impact on water.
00:33:18.270 --> 00:33:34.540
Cindy Bohlen: And during our ownership, VECO has worked to reduce its own internal water use from 31,000 to just over 26,000 gallons per day in its operations. And this is what we would call its footprint.
00:33:34.630 --> 00:33:41.290
Cindy Bohlen: And this is despite significant growth, so its water intensity has also dropped dramatically.
00:33:41.680 --> 00:33:46.120
Cindy Bohlen: Vigo's larger impact, however, comes from its handprint.
00:33:46.310 --> 00:34:04.279
Cindy Bohlen: And that's because its equipment is designed to optimize FAB yield. So it… its equipment optimizes and increases the number of chips coming out of the FAB on any given day.
00:34:04.360 --> 00:34:23.809
Cindy Bohlen: And this is extremely important, because an average chip manufacturing facility can use 10 million gallons of ultra-pure water each day. And that's the equivalent of the daily water usage of about 33,000 US households.
00:34:23.810 --> 00:34:30.190
Cindy Bohlen: So, Vigo's handprint is very important as a way to steward water.
00:34:30.330 --> 00:34:44.959
Cindy Bohlen: And so, while we don't ever take credit for the improved efforts of our portfolio companies, it is our belief that our collaboration-informed engagement does play a role in generating this positive impact
00:34:45.469 --> 00:34:48.219
Cindy Bohlen: And so, thank you, and I'll turn it back to you, Matt.
00:34:50.389 --> 00:34:59.099
Matt Drvaric: Thank you, Cindy. Thank you, Nate, Adam, for your updates on the strategies and how we integrate water stewardship into our process. At this time, we'll open the floor for any questions.
00:35:00.469 --> 00:35:20.219
Matt Drvaric: I will say we did receive one in advance, and we've also had several clients talk to this question with us in meetings over the quarter, and it was, you know, have you seen any signs of the market broadening? And when you think about the portfolio and the volatility in AI-related holdings, how do you feel about your position inside of the portfolios?
00:35:21.600 --> 00:35:30.500
Adam Peck: Yeah, that's a very good question, and I think, I'll have, Cindy help me answer it, and Nathan, for that matter.
00:35:31.060 --> 00:35:32.540
Adam Peck: Yeah, the…
00:35:34.320 --> 00:35:42.619

Adam Peck: the broadening one, I'm hoping broadens more into profitability, as a… as a main factor, and again, just…
00:35:43.060 --> 00:36:00.189
Adam Peck: all we can do, in our job is to analyze history and then try to predict, what looks… what things look like moving forward, and so I do think you'll get a broadening on the profitability slide. But as it relates to, like, sectors.
00:36:03.030 --> 00:36:05.600
Adam Peck: You know, tech has… in… in…
00:36:05.750 --> 00:36:15.730
Adam Peck: particularly focused in tech, because software hasn't been doing great, since AI came to the forefront. It's really been hardware, and specifically in hardware, it's been semis.
00:36:17.050 --> 00:36:32.300
Adam Peck: you know, a lot of comparisons have been made to the internet build-out, and we put in our small-cap quarterly letter talking about this current build-out compared to previous, build-outs that… that,
00:36:32.450 --> 00:36:39.470
Adam Peck: made up a large percentage of GDP. And so this is starting to become comparable to the fiber build-out.
00:36:39.490 --> 00:36:52.699
Adam Peck: of the late 90s, to the electricity build-out of the last century, to the railroad build-out of a couple centuries ago. It is… we are not denying how big AI is and how much it'll structurally change
00:36:52.790 --> 00:36:58.370
Adam Peck: Not only the stock market, but the economy and everyone's jobs.
00:36:58.760 --> 00:36:59.680
Adam Peck: But…
00:37:00.190 --> 00:37:10.750
Adam Peck: This specific question wasn't asked, and you, you saw, a lot of our performance driven by tech names. And in…
00:37:11.200 --> 00:37:20.079
Adam Peck: Nathan mentioned we sold Automodin, which was an industrial name that helps… that has been driven by data center build-outs.
00:37:20.340 --> 00:37:25.389
Adam Peck: But we've continued trimming, so on a year-to-date basis,
00:37:25.420 --> 00:37:36.670
Adam Peck: as all this stuff has gone up and up and up, we've been really paring back quite a bit. So while the IT weights, are still pretty high, it's because we…
00:37:36.670 --> 00:37:45.680
Adam Peck: We kept paring back, and we've been distributing that capital into other sectors, which we have just recently,
00:37:47.400 --> 00:37:55.320
Adam Peck: I'm trying to, you know… what was… I'm forgetting the name of the most recent model out of China. I want to say Mimi.
00:37:57.850 --> 00:37:58.990

Adam Peck: Mikkei,
00:37:58.990 --> 00:38:00.989
Cindy Bohlen: Kimmy K.
00:38:00.990 --> 00:38:11.270
Adam Peck: Or Kimmy! Kimmy! Sorry. So many names remember. Kimmy, you, that plus the, market starting to…
00:38:11.270 --> 00:38:22.720
Adam Peck: be disappointed with increased CapEx numbers from the hyperscalers. So you saw it last week, I think both Meta and Google declined on higher CapEx numbers.
00:38:22.880 --> 00:38:27.760
Adam Peck: So you're starting to see… And we had…
00:38:28.050 --> 00:38:44.760
Adam Peck: some internal things going on with some hedge funds that were heavily levered. But I do believe we're starting to see capital flow with a rotation from these… the really tight focus of AI into other sectors like healthcare, and insurance.
00:38:45.220 --> 00:38:47.040
Adam Peck: So,
00:38:48.450 --> 00:38:58.590
Adam Peck: at the end of the day, yes, I think we are seeing a broadening, and I'll certainly, Cindy and Nathan, you can add anything to that, that question.
00:38:59.310 --> 00:39:15.620
Cindy Bohlen: Yeah, no, I think that's right. I mean, tech obviously became a very crowded trade during the quarter, and a lot of the names went parabolic, and, you know, we were glad to participate in that, and as Adam said, we started to trim back our exposure, you know, several times as…
00:39:15.620 --> 00:39:20.270
Cindy Bohlen: The weights got high, and we felt our exposure was in a crowded space.
00:39:20.340 --> 00:39:33.250
Cindy Bohlen: And so, as the unwind has started to occur for various reasons, including some, like, the leveraged exposure to some of those spaces.
00:39:33.250 --> 00:39:48.690
Cindy Bohlen: you know, we were starting to put money to work in other places related to AI, because we do believe that AI has a long tailwind, but it's going to be seen in other areas, like robots and using AI to get better outcomes.
00:39:48.690 --> 00:40:13.310
Cindy Bohlen: hence our positioning in a name like Digi, which Nate talked about, you know, they use connectivity to make farming more efficient. So we've broadened not only in technology, we've gotten in some security software, cybersecurity names, too, because there's been a lot of need for that, but also into other sectors. And we think other investors are doing the same thing. We've started to see this broadening
00:40:13.310 --> 00:40:28.030
Cindy Bohlen: occur into, like Nathan just added to some insurance names. We're seeing it in healthcare and other areas because, you know, that crowded trade, that money has to go somewhere as others are taking profits or deleveraging to that

00:40:28.030 --> 00:40:31.259

Cindy Bohlen: The theme, and so we're starting to do the same thing.

00:40:34.970 --> 00:40:54.280

Matt Drvaric: Thank you, Cindy. That concludes the questions for today. As we wrap up, I'd like to iterate 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.

00:40:54.280 --> 00:41:04.530

Matt Drvaric: If you have additional questions and would like to speak with a member of the team, please don't hesitate to reach out. We look forward to connecting again next quarter, and enjoy the rest of your summer.