Walthausen Select Value Fund

Quarterly **Fund Commentary**

Ticker Symbols: Institutional Class WSVIX | Retail Class WSVRX

As of June 30, 2016

Environment

The second quarter was abnormally quiet. After the plunge and rebound in oil and most commodities and the signs of an imminent meltdown in China last quarter, US equity markets rose a bit with value leading the way, though much more of that was a search for yield in the Utilities and REITs rather that any search for fundamental value.

The US economy is giving mixed messages. We are pleased to see the steady decline in unemployment. We think that the many help wanted signs that we see on stores, restaurants etc. confirm that the government data is correctly painting the picture. We think that the loud and insistent pronouncements of a few older, wild haired gentlemen can be dismissed as political posturing, but yet the Federal Reserve continues to keep interest rates at unbelievably low levels. Frankly, we are in a low growth environment. The spurt in growth coming out of the financial meltdown of 2007-2008 was largely driven by a rebuilding of inventories, a surge in investment in shale gas & oil, and China's major infrastructure spending. Those are all passed. With excess capacity worldwide in most commodities and manufacturing, we cannot expect much growth from capital investment.

The good news is that the consumer is in good shape and the level of consumer debt is rising only modestly. Though mortgage debt is rising, the credit quality of the borrowers remains very high. Home equity lines of credit are low and credit card balances have been declining. The only area of concern is the persistent increase and high delinquency of student debt. We see the same picture in corporate borrowing; yes it is hurting our bank holdings that rates are low and companies large and small are being conservative, but with consumers and businesses in good shape we think that it is most likely that the economy will continue to expand. We may have reached a point where wages start to move up and new minimum wage laws may accelerate that, but that would not be bad. Perhaps, with higher wages, the workforce participation will increase. If those things happen, interest rates will inevitably move toward more normal levels.

That being said, we are concerned with what higher interest rates will do to the stocks which we own; the picture is mixed. Balance sheets are strong and the valuations of our holdings are typical of the values which these companies have held over the recent decades. If interest rates move up more rapidly than the market expects, there is likely to be selling pressure overall, especially if higher rates quickly curb demand. We don't see that as likely in the next few quarters.

Performance Review

Portfolio Factors

The second quarter was dominated by two themes, the surge in prices of Energy and Materials stocks and the strength of the yield sensitive REITs and Utilities. The REIT sector gained 8.8% and the Utilities sector showed a 10.1% return while the Materials sector was up 12.8 % and the Energy sector showed a 13.2% return. Our absence from Energy, REITs and Utilities accounted for almost the entire 200 basis points drag from allocation. It was partially offset by an overweight in Materials but, just as we were absent from most of the best performing sectors, we were substantially overweight in two underperforming groups, Industrials and Consumer Discretionary.

It is not surprising that with the drag from allocation we trailed our benchmark badly. We should remind investors that we are consistently overweight the Industrials and Consumer Discretionary sectors and virtually always absent from Utilities and REITs. Our strategy is to build value via stock selection and we have found our philosophy and process generally most effective in the Consumer, Industrial, Healthcare, Banking & Insurance, Energy, Materials & Information Technology sectors, while we have tended to avoid the yield sectors. We plan to stick with that strategy, but if current extraordinarily low interest rates prove to be the norm in the future, that could prove to be a poor decision.

Our absence from the Energy stocks was a decision based on the high inventories of crude oil, gasoline, natural gas and coal. We think that this will keep pressure on energy prices to the point where developing new resources is at best marginally profitable. Given that all the wells do deplete over time (and the shale oil wells are depleting fast), we think that there will be a time that we again invest in energy stocks.

Stock Selection: Contributors

Our top five contributors were diverse with no one theme or sector standing out. The list of contributors was led by Primerica (PRI), a life insurance company with an expertise in small policies. We have successfully held this company for several quarters. The company had been spun off from Citibank in the aftermath of the financial crisis but without most of its existing book of policies. We correctly surmised that the profits would grow as that book was rebuilt. While the stock has done well and we have taken some profits, we believe that investors still do not understand the company.

GCP Applied Technologies (GCP) was the second largest contributor. The company is a spinoff from W.R. Grace and has an attractive portfolio of specialty chemicals that are highly valued in the construction industry. The stock benefited as investors began to understand the values and realized that via spinoff, the operation was no longer constrained by Grace's historical liabilities. That was followed by McGrath RentCorp (MGRC), Outfront Media (OUT) and PolyOne (POL). All are strong companies which we have known for a while and are showing steady progress. We did have one name, PrivateBancorp (PVBT), which was subject to a takeover. The company agreed to be acquired by CIBC, a leading Canadian bank. We have since sold that stock. It was the only one of the portfolio holdings which benefited from M&A activity in the quarter.

Portfolio Contributors – Q2 2016

Security	Average Weight (%)	Contribution
Primerica, Inc. (PRI)	2.85	0.73
GCP Applied Tech. (GCP)	2.70	0.71
McGrath Rentcorp (MGRC)	2.61	0.55
Outfront Media (OUT)	2.52	0.38
PolyOne Corp. (POL)	2.41	0.34

Stock Selection: Detractors

SeaWorld Entertainment (SEAS) proved to be a difficult holding in the quarter. While we are pleased with management, the stock was punished as attendance in all the theme parks fell short of expectations. We are sticking with the position because we believe that American workers are seeing improving incomes and balance sheets and thus are more likely to visit the parks, and because we believe that the company is positioned to attract more visitors. Our performance was also impacted by our holding in Molina Healthcare (MOH). We concluded that management had expended too aggressively and execution was suffering, and consequently elected to sell the position. We were also hurt by our holdings in Pitney Bowes (PBI) and ITT (ITT). Both of these are relatively new holdings and we continue to be convinced that management can build value. In the case of Pitney Bowes, we believe that they are effectively adding services (some by acquisition) to their already strong position as a global leader in providing postage meters. In the case of ITT, this former conglomerate slimmed down via sales and spinoffs and has become a very strong and highly profitable player in the pump and valve markets. We continue to be convinced that these are good investments.

The last of the meaningful detractors was GNC Holdings (GNC), a retailer of vitamins and supplements with a very strong position in its market place. We are pleased with the strategy of using cash flow and proceeds from franchising of retail outlets to reduce debt and repurchase shares. Unfortunately, the stock has suffered as management's efforts to improve same store sales have not proved to be effective.

Portfolio Detractors – Q2 2016

Security	Average Weight (%)	Contribution
SeaWorld Ent. (SEAS)	2.12	-0.73
Molina Healthcare (MOH)	1.78	-0.56
GNC Holdings (GNC)	2.41	-0.55
Pitney Bowes (PBI)	2.20	-0.41
ITT, Inc. (ITT)	2.02	-0.36

Portfolio Changes

During the second quarter, we added five new holdings. They are all from different industries but can be characterized as very strong companies with clear market and operational strengths. Moog (MOGA) is a producer of specialty equipment which goes into aerospace and industrial applications. In the past decade they have expanded into energy and medical applications. Westlake Chemicals (WLK) is a very strong low cost maker of ethylene and related products. Polaris (PII), a leading maker of all-terrain vehicles, motor cycles and snow mobiles was also added to the portfolio as the stock weakened on what we think are ill-founded concerns about the US consumer as well as the effects of a warm winter on the snowmobile business and some imbalance in the portfolio. We added Seaboard (SEB) because this large pork producer is now effectively turning its joint venture in Butterball turkey into a winner. We also established a position in Restoration Hardware (RSTO). The retailer of stylish furniture, hardware and fixtures stumbled and the stock dropped sharply as a result of a poorly executed introduction of a new line. They were unable to meet customer demand for delivery and thus incurred excess delivery costs and discounted accounts of unhappy customers. While that is not laudable, it has given us an opportunity to buy the stock in a good company at what we believe is a big discount to its value.

Exhibit 1: Sector Allocation - % over/underweight vs. Russell 2500 Value Index

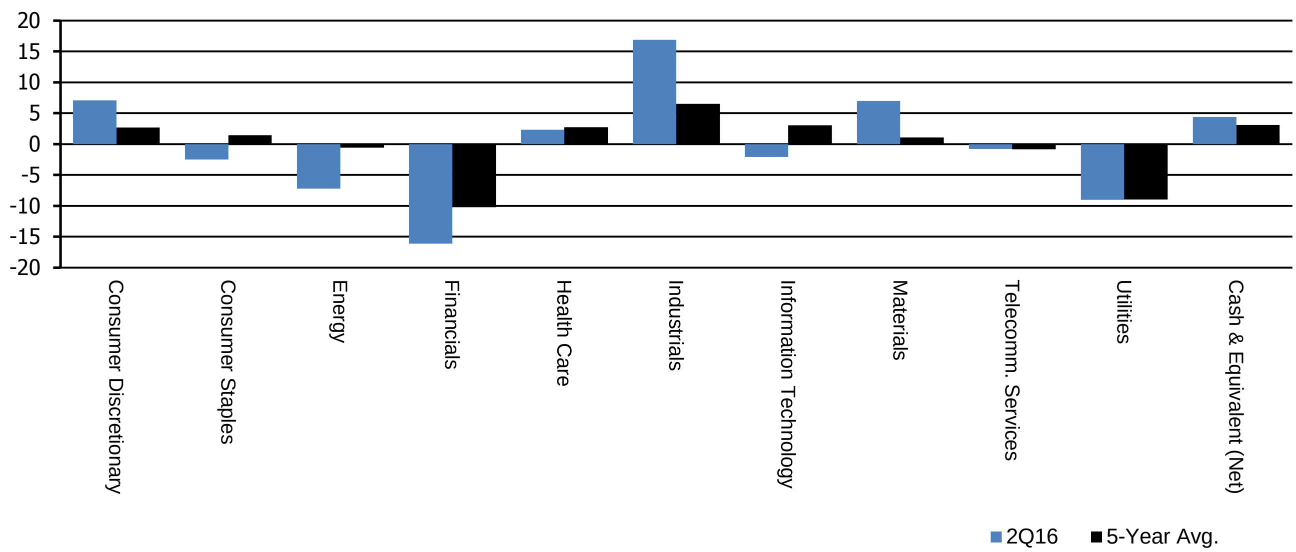

Exhibit 1 above highlights the fact that sector weight differentials between the Fund and the Russell 2500 Value Index benchmark have not changed greatly from today's levels versus the five year average.

Outlook

While the year started out on a note of fear, the economy seems to be expanding slowly and pretty steadily. Interest rates continue to be unsustainably low but, for the time being, likely to stay there. Our holdings are concentrated in strong companies with good business models and strong balance sheets. The markets have avoided a bear market which seemed to be developing late last year and early this year.

While we do not see the valuations of the stock that we own as excessive, we understand that the market and all the stock within it are vulnerable when interest rates move back toward normal level. We think that because of our avoidance of yield stocks, we are less vulnerable to the effect of such an event than our benchmarks.

Top Ten Holdings (%)

Primerica, Inc.	3.1
Deluxe Corp.	3.1
McGrath Rentcorp	2.9
La-Z-Boy Inc.	2.9
HealthSouth Corp.	2.8
AptarGroup Inc.	2.8
Outfront Media, Inc.	2.7
GATX Corp.	2.7
GCP Applied Technologies, Inc.	2.7
Clean Harbors, Inc.	2.6
Total % of Portfolio	28.3

Fund Statistics

	Fund	Russell 2500 Value Index
Number of Holdings	40	1716
Median Market Cap (Billions)	$2,919.9	$824.6
Weighted Avg. Market Cap (Billions)	$2,960.7	$3,746.2
Price/Book[2]	1.8	1.4
P/E using FY1 Est[3]	14.4	16.0

Source: FactSet Research

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Portfolio Performance

	Q2 16	1 Year	3 Year	5 Year	Since Inception (12/27/10)
Walthausen Select Value Fund: Institutional Class	1.33	-5.43	5.41	9.47	9.33
Walthausen Select Value Fund: Retail Class	1.27	-5.63	5.17	9.18	9.05
Russell 2500 Value Index[1]	4.37	0.22	8.14	9.59	9.85

Total Expense Ratio: 1.45%. Expense ratio per the June 1, 2016 prospectus.

Performance data quoted represents past performance and does not guarantee future results. Investment returns and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. The current performance may be lower or higher than the performance data quoted. Investors may obtain performance data current to the most month-end by calling (888) 925-8428. Periods over one year are annualized.

[1]The Russell 2500® Value Index measures the performance of the small cap value segment of the U.S. equity universe. It includes those Russell 2500 companies with lower price-to-book ratios and lower forecasted growth sales.

The Net Expense Ratio includes a waiver. The Advisor has contractually agreed to waive, for the Institutional Class Shares through May 31, 2017, 0.25% of the 0.45% Services Agreement fees applicable for Fund average daily net assets up to $100 million. The Advisor may not terminate the fee waiver before May 31, 2017. From the prospectus dated June 1, 2016.

Disclosures

[2]Price/Book measures the weighted average of the price to book value of all the stocks in the fund's portfolio, excluding companies with negative book values. Book value is the total assets of a company less total liabilities.

[3]P/E using FY1 Estimate is a ratio reflecting the amount of earnings estimated for next year per dollar of amount share price. For the fund, the individual P/E stock ratios are then weighted by their portfolio and market values to calculate a weighted average for the portfolio as a whole. Companies with negative earnings are excluded from the calculation. This ratio is not a forecast of the fund's future performance.

An investment in the Fund is subject to investment risks, including the possible loss of the principal amount invested. The Fund invests in the stocks of small capitalization companies, which may subject the Fund to additional risks. The earnings and prospects of these companies are generally more volatile, and they may experience higher failure rates than do larger companies. Their stocks are subject to a greater degree of volatility, trade in lower volume and may be less liquid. Investment in the Fund is also subject to common stocks risk, value investing risk, sector risk, securities lending risk, and investment management risk. Fund holdings and asset allocations are subject to change and are not recommendations to buy or sell any security.

Investors should consider the investment objectives, risks, charges and expenses of the Fund carefully before investing. The prospectus contains this and other information about the Fund. You may obtain a prospectus by calling (888) 925-8428. The prospectus should be read carefully before investing. Distributed by Rafferty Capital Markets, LLC – Garden City, NY 11530, Member FINRA.

Contributors and detractors performance data and analytics provided by FactSet. To measure performance for periods when portfolio holdings change, portfolio analysis calculates the security weights and returns on a daily basis, then geometrically link returns across the measurement period.

Walthausen Funds
(888) 925-8428
www.walthausenfunds.com