Environment

2020 has been a memorable year. The market's reaction to the pandemic onset and a gradual moderation of the virus's spread in the first half seemed rational, but we were surprised by the strengthening of the market as the virus came back with a vengeance in the fall and the country divided in a most bitter election year. As people were increasingly worried and angry, the market continued to gain strength. Now there are various theories about why this optimism drove the market to all time highs. Most of these are based on sophisticated and detailed analysis of all the quantifiable factors which can affect the market. We, however, do take note that the market is a social phenomenon. People are willing to buy, own and sell securities based on a common trust. With optimism and trust seemingly at a low level, we question what is happening. We don't know but observe that prices are rising in most assets including homes, commodities and Bitcoins. Paul Tudor Jones' endorsement of Bitcoins is an explicit statement of distrust in currency. Perhaps that is the key. While we commonly understand inflation as a product of excess demand, we need to understand it also as a devaluation or debasement of the currency. Thus far, the statistics suggest that wage inflation is not an issue. However, when we talk to management, we do ask about wages and worker availability and have been surprised that several of the companies that we own have reported shortages of labor and that wage increases, particularly in jobs which require only low skills, are accelerating.

As we look forward the outlook is hazy. The economic dislocation from Covid19 has had dramatic but uneven impacts on the country. The election, including the decisive results from the Georgia Senate runoff, appear to give the Democratic Party a strong position to put their programs in place. However, it is already apparent that there is not one, but a large menu of programs. The legislative majorities are slim and the new administration will have their hands full accelerating the vaccine program and dealing with a weak economy. We don't know what other programs will be put in place. With that in mind we default to our best strategy; that is to continue to search for companies where our analysis leads us to expect earnings and cash flow that are meaningfully better than what the market price of the stock suggests. We expect that will produce superior returns but acknowledge that the market has evolved from a market of stock selection to a factor driven market. Our emphasis has always been on improving returns on invested capital, generation of excess cash and lack of investor enthusiasm. Those factors have worked well for us for many years, but in recent years the returns to our investors have been unimpressive. We think that our strategy which amounts to buying companies that are likely to do better and buying at discount prices is just good business. We, however, have no insight regarding when the factor preferences in the market will shift in our favor.

Portfolio Performance

<u>Portfolio Factors</u>

For the Fund, the fourth quarter was very disappointing. It was an extraordinarily good period for the US equity markets with a dramatic shift to small cap stocks as seen in a 31.4% gain for the Russell 2000 small cap index versus an impressive but more moderate 10.4% gain for the Russell Top 50 Mega Cap Index. We have been commenting on the dominance of the large growth stocks for way too long. As dramatic as the shift was, small cap value continued to be a big loser for the year with a gain of only 4.6% for the Russell 2000 Value benchmark compared to a gain of 39.3% for the Russell Top 200 Growth Index. When we look at the details of which stocks did well in the fourth quarter, we saw a burst of irrational speculation. We saw a lot of failed growth stocks, companies that had never made money, and were very correctly down from their highs, and which by virtue of their low prices and a low price to book value, were classified as "value" stocks, even though in our analysis these companies have a surplus of optimism and an absence of value. They do not have valuable business models and don't own valuable assets. It was not a rally of value stocks but a burst of irrational optimism as the country was heading toward a "dark winter". It is unusual behavior but not unprecedented. The combination of great fear, interest rates well below the inflation rate, and a distrust of the currency all came together in a crazy quarter.

Our attribution analysis showed that virtually all of our underperformance came from stock selection. If you disregard the substantial performance drag of having 3.75% in cash, which cost us 117 basis points in performance, it was all due to selection; but first, let's talk about which sectors did well and which dragged; that may help explain the quarter. The best performing sector for the benchmark index was Energy. Due to falling prices of petroleum and natural gas, the sector had been terrible for most of the year, with a number of much-loved stocks disappearing into Chapter XI reorganization. Worldwide, there is excess petroleum production. Although prices have stabilized a bit, they are not at levels that make it easy on the energy companies. We were a bit underweight with our holdings in two financially strong Marcellus based natural gas producers and one transportation company. We did well with Seacor Holdings (CKH), the transportation company, as the company agreed to be acquired. The natural gas companies underperformed the sector. We continue to be optimistic about the outlook because the rate of drilling for gas has dropped and these two firms are well endowed with good acreage and are very efficient at developing this resource.

The second best sector for the benchmark was Materials. We were out of the loop. Even though we had holdings in five stocks and a 4.5% weight, versus 6.3% for the benchmark, we missed the boat with only a 7.2% gain versus the benchmark sector's gain of 46.6%. We did not anticipate that, in spite of a slack world economy, metals and other commodity prices would soar. Our holdings are companies who convert metals and basic chemicals to higher value prices and thus do not benefit from rising raw materials prices. They operated well but the stocks which had performed well through the first nine months languished in the last quarter.

The next best performing sector was Information Technology; that sector returned a laudable 43.6%. Unusually, we were well overweight, but our selections, despite strong absolute performance, trailed the benchmark sector with a 34.8% gain. Our selections in the sector followed our usual pattern of selecting the reliable and strongly profitable companies, a number of which we have closely followed for a considerable period of time. Our holdings are not at the cutting edge of innovation. They are largely providers of components, systems, production equipment and manufacturing services which support the digital world. The companies did well and the stocks did better than our benchmark but trailed the sector's performance.

Stock Selection: Contributors

Our five best performing names for the quarter included two banks; First Bancorp (FBNC) and Pinnacle Financial Partners (PNFP). This was a pleasant surprise. Though we saw potential in the community and regional banks after observing that the stocks were down over worry that the current economy would devastate the banks the way that the Great Recession did, our research confirmed that the banks were financially stronger, that they were not extended into any particular area that had high risk like questionable mortgages, and that the combination of the Payroll Protection Program of the CARES Act and the Federal Reserve's forceful intervention in credit markets, all made for a relatively benign environment for the banks.

Although we see bank stocks as defensive, they performed quite well in the quarter.

The best single performing stock was Ameresco (AMRC). The company has built an impressive record in engineering secure clean energy grids. They have compounded the value of this expertise by selectively/profitably investing in these projects. The stock has done well. We have sold some of the position to keep the holding in balance with the portfolio but continue to see an attractive future for the company. The other two top performers were Kulicke & Soffa (KLIC), a producer of assembly equipment in the semiconductor field, and Great Lakes Dredge & Dock (GLDD), which provides dredging services. In the case of Kulicke, the stock price did well as the market demand for semiconductor equipment picked up. The dredging market is also doing well but we credit Great Lake's performance to increased attention by management, upgrading equipment and good strategic bidding on projects. We continue to hold positions in all those names mentioned.

Portfolio Contributors – Q4 2020

Security	Average Weight (%)	Contribution
Ameresco, Inc. Class A	2.46	1.29
First Bancorp	2.11	1.25
Pinnacle Financial Partners, Inc.	1.83	1.22
Kulicke & Soffa Industries, Inc.	2.15	0.95
Great Lakes Dredge & Dock Corp.	2.71	0.94

Stock Selection: Detractors

The worst performing sectors were Utilities, Real Estate and Healthcare. We are typically underweighted in utilities and real estate and that was true in the quarter, although we are starting to see more opportunities in real estate as our detailed analysis shows some good properties selling at attractive prices. The low weighting in the sector helped performance but our too conservative selections more than offset that gain. In healthcare, we did do well with a weight of only 1.8% compared to 6.5% for the benchmark sector. Our selections came out well, with BioTelemetry (BEAT) being acquired at a good premium. Healthcare had been a star sector through the year and we had struggled to find companies which met our criteria. Toward the end of the year, the wilting prices of healthcare stocks have provided some opportunities.

With the performance so poor, we naturally looked for the stocks that were disasters. We did not find that to be the case. Of the bottom 10 contributors, six were stocks that we added in the last month of the quarter and their performance in the short period was unimpressive due to timing of the purchases. Of the other four, the one that I called a disaster was FreightCar America (RAIL). This railcar builder concluded that their attempts to achieve profitability in a large and modern plant in Alabama, their only plant, were not succeeding and they chose to shift production to a startup joint venture in Mexico. The decision was costly and the financing to do the change is very burdensome. As terrible as that was, this relatively small holding penalized performance by only 13 basis points. Two companies which had a good first nine months, and which still see a strong demand, are 1-800-Flowers.com (FLWS) and M/I Homes (MHO). In the case of Flowers, we sold the stock as it became apparent that the boom in direct to home deliveries of virtually everything was placing a burden on their systems, and the rapid deliveries that are their core, could be challenged. M/I Homes is a bit challenged by the prospect of a climb in interest rates. We have retained the holding as we believe that in the environment of cash being worthless and home prices rising at well above interest rates, home purchases will continue to be strong for at least the next several years. We also realized a poor return on our investment in Kimball International (KBAL). We sold the stock after analyzing a meaningful acquisition. We were cautious that integrating this acquisition could prove to be a sizeable challenge.

Portfolio Detractors – Q4 2020

Security	Average Weight (%)	Contribution
1-800-Flowers.com, Inc. Class A	1.10	-0.36
Accuray, Inc.	0.21	-0.13
FreightCar America, Inc.	0.12	-0.13
Big Lots, Inc.	0.31	-0.11
M/I Homes, Inc.	1.18	-0.07

Portfolio Changes and Positioning

The portfolio continues to be well positioned with a diversified portfolio of stocks in companies where we are comfortable that their managements have good potential for long term value building. During the quarter, we were fairly active, adding ten new positions and exiting nine. We have already mentioned Seacor and BioTelemetry, which were sold after they agreed to be acquired. We also mentioned our decisions to sell Kimball international, 1-800-Flowers and FreightCar America because of concerns regarding recent developments at those companies. We also sold our position in PC Connection (CNXN). We had felt that the company was better positioned in the market to do well in this period of social isolation. We also sold Darling Ingredients (DAR), DXP Enterprises (DXPE) and Atkore International (ATKR) after those stocks reached our price targets.

We purchased positions in ten companies. We found three promising stocks in the Consumer Discretionary sector. Monro Muffler Brake (MNRO) and Big Lots (BIG) are both well known to us. We are pleased with corporate initiatives that have been made at both these companies. We also saw a good opportunity in Perdoceo Education (PRDO), a for profit higher education company focused correctly on preparation for careers where there is good sustainable demand for trained employees.

We added CNX Resources (CNX) to strengthen our exposure to natural gas production from the Marcellus fields. It is one of the highly efficient, well financed exploration and production companies that we mentioned earlier. We found two promising healthcare companies, Accuray (ARAY) and NuVasive (NUVA). Our enthusiasm in both of these companies was ignited by the promise of new products which they are bringing to the market. We added Axcelis Technologies (ACLS), a firm which makes equipment for preparing silicon wafers in the production of semiconductors. We also added positions in NMI Holdings (NMIH), Ampco Pittsburgh (AP) and VSE Corp. (VSEC).

The portfolio continues to have a market cap that is significantly smaller than that of the Russell 2000 Value Index benchmark. The portfolio's weighted average market cap is now about 55% of our benchmark's weighted average market cap. This is by design as we believe that the smaller market caps receive less attention and thus the stocks are more likely to trade less efficiently. We look at that as a competitive advantage. As is typical, the returns on assets and returns on equity, net margins and estimated 3-5 year growth rates exceed the benchmark. Even so, the P/E ratio is slightly lower.

Walthausen Small Cap Value Fund

Quarterly **Fund Commentary**

Ticker Symbols: Institutional Class WFICX | Investor Class WSCVX

As of December 31, 2020

Exhibit 1: Sector Allocation - % over/underweight vs. Russell 2000 Value Index

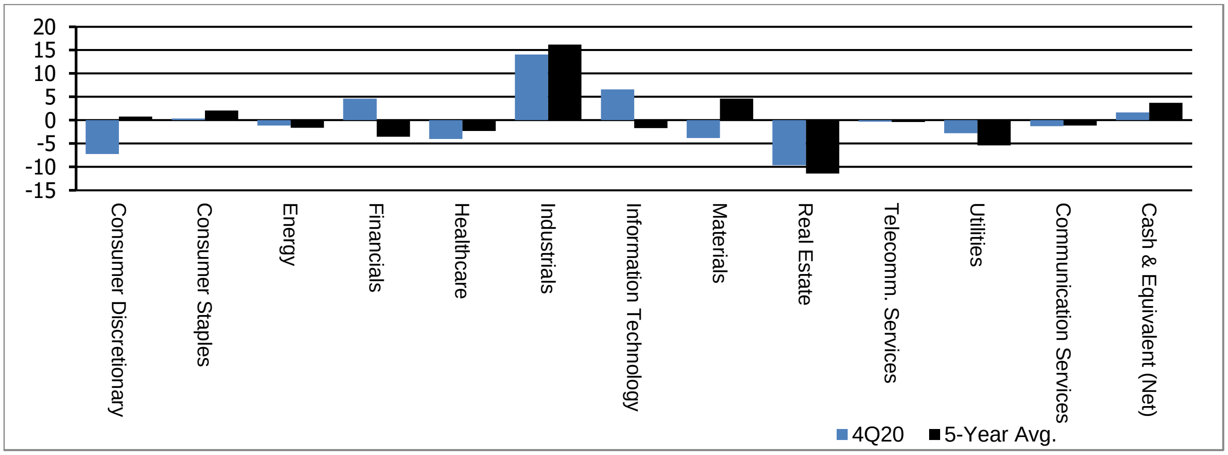

Exhibit 1 above highlights the fact that sector weight differentials between the Fund and the Russell 2000 Value Index benchmark have not changed greatly from today's levels versus the five year average.

Top Ten Holdings (%)

Great Lakes Dredge and Dock Corp.	3.0
Monro Muffler Brake, Inc.	2.7
AZZ, Inc.	2.6
UMH Properties, Inc.	2.5
Landec Corp.	2.3
Textainer Group Holdings Ltd.	2.2
Miller Industries, Inc.	2.1
City Holdings Co.	2.0
Ameresco, Inc.	2.0
Pinnacle Financial Partners, Inc.	2.0
Total % of Portfolio	23.4

Fund Characteristics	**Fund**	**Russell 2000 Value Index**
Number of Holdings	63	1,486
Return on Equity[1]	9.7	4.8
Weighted Avg Market Cap (Millions)	$1,372	$2,462
Price/Book[2]	1.6	1.4
P/E using FY1 Estimate[3]	14.7	15.7
Long Term Debt/Total Capitalization[4]	27.4	39.6
Information Ratio (TTM)[5]	.54	-
Active Share[6]	95.5	-

Source: FactSet Research

Portfolio Performance

	Q4 20	**1 Year**	**3 Year**	**5 Year**	**10 Year**	**Since Inception**	**Inception Date**
Walthausen Small Cap Value Fund: Investor Cl	27.27	-0.11	-0.81	7.17	7.98	10.09	2/01/08
Russell 2000 Value Index[7]	33.36	4.63	3.72	9.65	8.66	7.36	
Walthausen Small Cap Value Fund: Institutional Cl	27.40	0.17				10.05	12/31/18
Russell 2000 Value Index[7]	33.36	4.63				13.17	

Total Expense Ratio: 1.30% for Institutional Class, 1.30% for Investor Class. Net Expense Ratio: 0.98% for Institutional Class, 1.21% for Investor Class. Expense ratio per the June 1, 2020 prospectus.

The Net Expense Ratio includes a waiver. The Advisor has contractually agreed to waive Services Agreement fees and Management Fees to the extent necessary to maintain total annual operating expenses of the Institutional Class shares and Investor Class Shares, excluding brokerage fees and commissions, taxes, borrowing costs (such as (a) interest and (b) dividend expenses on securities sold short), the cost of acquired funds and extraordinary expenses at 0.98% and 1.21% respectively, of its average daily net assets through May 31, 2021. The Advisor may not terminate the fee waiver before May 31, 2021. The Trustees may terminate the expense waiver upon notice to the Advisor. From the prospectus dated June 1, 2020.

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.

Disclosures

[1]Return on Equity (ROE) is a measure of financial performance calculated by dividing net income by shareholders' equity. ROE is a measure of how effectively management is using a company's assets to create profits.

[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.

[4]Long Term Debt/Capitalization is a ratio that measures the proportion of long term debt used to finance assets, as a percentage of the firm's total capitalization.

[5]The Information Ratio is a measurement of portfolio returns beyond the returns of a benchmark, in this case the Russell 2000 Value Index, compared to the volatility of those returns.

[6]Active Share is a measure of the percentage of portfolio holdings that differs from the benchmark index.

[7]The Russell 2000® Value Index measures the performance of the small cap value segment of the U.S. equity universe. It includes those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth sales.

[8]The Russell 3000® Index tracks the performance of the 3,000 largest U.S.-traded stocks which represent about 98% of all U.S incorporated equity securities

[9]The Russell Top 200® Growth Index measures the performance of the especially large cap segment of the U.S. equity universe. It includes those Russell 200 Index companies with higher growth earning potential.

[10]The Russell Top 50® Mega Cap Index measures the performance of the largest companies in the Russell 3000 Index It includes approximately 50 of the largest securities based on a combination of their market cap and current index membership and represents approximately 40% of the total market capitalization of the Russell 3000.

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.

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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
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