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DF Dent All Cap Growth Strategy

July 2017 Commentary

Portfolio Thoughts

Most major U.S. stock market indices gained in the second quarter of 2017, as the year has exceeded our expectations for equity returns. The D.F. Dent All Cap Growth strategy returned 8.5% for the second quarter of 2017, outperforming the Russell 3000 Growth Index which returned 4.7%. The strong second quarter puts our year to date performance at 16.7%, outperforming the Russell 3000 Growth Index return of 13.7%.

Performance for the second quarter was positively impacted by stock selection in the Technology, Industrial, Health Care and Real Estate sectors. Technology stocks continued their strong advance from the first quarter as 8 of the 11 Technology holdings appreciated by double digits in the second quarter. Performance was also helped by being underweight the Consumer Staples, Consumer Discretionary, and Energy sectors. These positive contributors were offset slightly by stock selection in the Consumer Discretionary and Financial sectors.

2Q17

Ticker		Contribution To Return
	5 Highest	**2.85**
ISRG	Intuitive Surgical, Inc.	0.74
CSGP	CoStar Group, Inc.	0.58
ROP	Roper Technologies, Inc.	0.57
WAB	Westinghouse Air Brake Technologies	0.50
ANSS	Ansys, Inc.	0.46
	5 Lowest	**-1.46**
IMAX	IMAX Corporation	-1.01
DFS	Discover Financial Services	-0.24
WAGE	WageWorks, Inc.	-0.16
EXPO	Exponent, Inc.	-0.01
MKL	Markel Corporation	-0.00

The top three contributors during 2Q were:

- **Intuitive Surgical, Inc. (ISRG)**, a leading designer and manufacturer of robotic surgical systems, outperformed in first quarter as the company reported very strong organic growth driven by strong procedure volume growth both inside the U.S. and outside the U.S. ISRG raised its full year guidance as a result of the strong first quarter. In addition, ISRG announced the launch of da Vinci X system which will likely be well received by customers. This, combined with the upcoming launch of the da Vinci Sp system and the development of a "flexible robotics" system, set ISRG up for healthy growth over the next several years. We trimmed ISRG on the stock's strength in the second quarter.

- **CoStar Group, Inc. (CSGP),** the leading provider of information, analytic and marketing services to the commercial real estate market, reported first quarter results that surpassed analyst expectations across the board. After disappointing investors with increased expenses and lower profitability in 2016, these results provided investors with some confidence in CoStar's ability to achieve their long-term goals. Specifically, net new bookings were up nicely from the previous quarter. The LoopNet integration was completed and the salesforce was trained and ready to begin selling in the 2nd quarter. Also, the new facility in Richmond, VA was not only well ahead of schedule in hiring, but also in productivity. After increasing our position size in the market sell off in February of 2016 at attractive prices, we reduced the position after the recent outperformance in the quarter.

- **Roper Technologies, Inc. (ROP),** a provider of niche software, health care, and industrial products, posted very strong 1Q earnings. ROP benefitted from (1) accretion as a result of its recent acquisitions of Deltek and ConstructConnect and (2) improved organic growth due to the ebbing of foreign exchange and energy-related headwinds. ROP's +5% organic growth report was the strongest figure in eight quarters. We added to the stock twice at much lower prices in 2016, and then we made two trims on strength in the 2Q to rebalance the position downward.

The top three detractors during 2Q were:

- **IMAX Corporation (IMAX),** a global provider of premium cinematic content and theater systems, reported global box office results below expectations in the second quarter. While IMAX management maintains this softness is a movie-content-specific problem, the market's concern that there is a more systemic issue, caused downward pressure on theater stocks, including IMAX, during the quarter. During the quarter we trimmed the position and we are evaluating future moves.

- **Discover Financial Services (DFS),** a leading direct banking and payment services company, gave back most of the gains it experienced in late 2016 following the U.S. Presidential election. We trimmed the position on strength in November following the election. Despite reporting quarterly earnings that met expectations and loan growth that exceeded expectations, Discover's stock declined in response to reduced market expectations for U.S. GDP growth and corporate tax reform/reductions, the latter of which would have a material impact on a full-tax-rate payer such as DFS. In addition, some of Discover's stock weakness is attributable to sequentially higher loan delinquencies that accompanied its faster loan growth.

- **WageWorks, Inc. (WAGE),** an administrator of consumer-directed benefit accounts for employers, continues to perform very well operationally and to deliver impressive revenue and earnings growth. The stock, however, may have gotten a little ahead of itself in 2016 and seems to be in a consolidation mode thus far in 2017. The integration of the ADP consumer-directed benefits business seems to be going smoothly, and the sales and M&A pipelines appear to be active. We attribute the stock weakness to valuation concerns rather than operational concerns. We added to WAGE in the second quarter following relative underperformance after trimming at higher prices in January.

Eighteen stock positions, almost half the D.F. Dent All Cap Growth portfolio, were up over 20% and the top five performing names have returned over 35% year-to-date. Many of these top performing stocks have experienced periods of flat returns in recent years due to increased long-term investments, which resulted in short-term pressure on growth or margins. Rather than sell these stocks and risk missing the upside, we maintained and, in many cases, added to our positions in these stocks through the flat period because of our confidence in management and the strong prospects for long-term growth in the future. Over time, this strategy has benefitted your portfolio.

Red Hat (RHT), a leading open-source software company, is a good example of this strategy. The company has a strong core infrastructure business in Red Hat Enterprise Linux (RHEL). However, RHT has not rested on its laurels in its core business. It has, instead, invested very heavily for growth in emerging open-source technologies, including JBoss middleware, OpenStack and OpenShift, and has undertaken sales force expansion and geographic expansion. All of these investments sacrificed margin (and earnings growth) in the short term with the goal of extending strong revenue growth for many years. The stock declined -15.8% in 2016, and we added to the position twice at lower prices. RHT is seeing the revenue growth from these investments, and investors are beginning to understand the wisdom of RHT's growth strategy. For the first six months of 2017, the stock is up 37% and we recently trimmed the position.

Market Thoughts

The U.S. expansion is in its ninth year, making it the third longest expansion in the post-war era. We are now in a period when fundamentals may matter more than they have over the past few years. The rising tide may not continue to lift all boats. Margin expansion will be tougher to achieve. Management decisions, like handling rising labor costs, will be vital to a company's success. Your D.F. Dent portfolio is invested in high-quality growth equities, with excellent management teams that we think can successfully navigate this environment. We have spent time with these management teams and know how they think and operate. Additionally, the Technology and Financial sectors will deliver the fastest earnings growth in 2017 outside of the recovery in energy, and your portfolio is overweight both these sectors. We are focused on stocks that will deliver revenue and earnings growth. We continue to monitor our portfolio companies very closely and weight the portfolio in favor of those stocks with the best prospects for above average returns. We are being mindful to trim names that have done well and to rebalance the portfolio.

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We appreciate the confidence you have placed in D.F. Dent and Co. We will continue to work diligently on your behalf.

This commentary can be found on our website (www.dfdent.com). We encourage you to refer to our website for other information about our firm and our investment products, including our mutual funds, the DF Dent Premier Growth Fund (DFDPX), the DF Dent Midcap Growth Fund (DFDMX) and our new DF Dent Small Cap Growth Fund (DFDSX)