Small Cap Advantage

Portfolio Comments

December 31, 2020

Distinguishing Features

As of 12/31/2020, the Small Cap Advantage portfolio remains overweight in technology compared to the Russell 2000 Growth benchmark, 27.7% versus 18.4%. The portfolio is also overweight to the Index in industrials (17% versus 14%), financials (6% versus 4%), and energy (3.3% to 1.6%). At 14%, consumer discretionary is about equal-weight to the Index, as are real estate (3%) and basic materials (2%). The healthcare sector continues as the largest underweight (25% versus 34%). The portfolio currently has no exposure to the small telecom, utilities, and consumer staples sectors, where the Index weightings are 2%, 3%, and 3%, respectively.

Commentary

Market Environment

US markets posted another exceptional return in the 4th quarter. The markets were buoyed by several significant factors over the quarter: the cloud of uncertainty over the election was lifted, the FDA approved two vaccines and their subsequent initial roll-out began, and Congress finally passed another COVID-19 relief package. The coronavirus pandemic has caused a rewiring and modernization of companies in surprising ways, serving up unexpected opportunities for some to prosper.

Performance Discussion

In the 4th quarter, the Small Cap Advantage composite returned +36.0%, net of fees, well ahead of the +29.6% return of its Russell 2000 Growth benchmark. Year-to-date, the portfolio has returned +65.0%, net of fees, versus +34.6% for the Index. In the quarter, strong stock selection in technology led performance, boosted by the portfolio's overweighting of the sector. Selection in consumer discretionary, industrials, basic materials, and real estate also contributed nicely. Our overweight position in energy more than offset negative selection in the sector. Our lack of exposure to utilities, consumer staples, and telecom was a plus. Selection in healthcare and financials weighed on performance.

With respect to LifeCycles, the Pioneer and Core Growth LifeCycle categories soundly outperformed the Index, while the Special Situation category's return lagged the Index by 2%. Three technology names were in the top five, representing all three LifeCycles: **Magnite** (Pioneer), **Brooks Automation** (Special Situation), and **Workiva** (Core Growth). **Enphase Energy** (Core Growth, energy) and **Chart Industries** (Special Situation, industrials) were also in the top five.

On the negative side, the largest detractors included three Pioneer holdings: **Esperion Therapeutics** (healthcare), **eHealth** (financials), and **CryoPort** (industrials). Two Core Growth names were also in the bottom five: **CoStar Group** (real estate) and **Cardiovascular Systems** (healthcare).

Outlook

Over the course of the Russell 2000 Growth's history, there have been very few quarters where the Index has returned greater than 29%. In 2020, we have had two quarters above this outstanding return. Pioneers have been the best performing category in the portfolio; we have been trimming the winners and adding to names in other LifeCycle categories.

The returns achieved in 2020 would have been extraordinary in any year, let alone during a global pandemic. The market is forward looking, though government stimulus, near 0% interest rates, retail investors returning to the markets in droves, and historically high level of margin debt have all played a part in the market rise. For the Advanage portfolio, as bottom-up investors, we will continue our strict adherence to our discipline processes to select out the companies across LifeCycles that demonstrate superior fundamental factors no matter the market environment. Our valuation tools will guide us to invest in the stocks of those companies when risk/reward is attractive.