POLEN | CAPITAL

POLEN U.S. SMALL COMPANY GROWTH STRATEGY

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Summary

- During Q2 2019, the Polen U.S. Small Company Growth Composite Portfolio (the "Portfolio") returned 6.56% gross of fees. This compared to a return of 2.75% for the Russell 2000 Growth Index (the "Index") in the same period. For the trailing 12-month period, the Portfolio returned 12.85% gross of fees compared to -0.47% for the Index.
- In the second quarter of 2019, global markets continued higher after the strong rebound in the first quarter with periods of volatility tied to headlines about trade and more accommodating monetary policy from central banks. Two macro factors that many of our portfolio companies are dealing with are wage inflation for service-related jobs and tariffs, and we believe our companies are managing these risks well.
- Performance this quarter was driven entirely by stock selection, especially in the technology and healthcare sectors and by some of our largest holdings including Globant, Fox Factory, and Pool Corporation. Gains were partially offset by weakness in a single stock, Stamps.com.
- Our companies continue to perform well, exhibiting above-average growth rates, high returns on invested capital, and low levels of financial leverage.

Commentary

During Q2 2019, the Polen U.S. Small Company Growth Composite Portfolio (the "Portfolio") returned 6.56% gross of fees. This compared to a return of 2.75% for the Russell 2000 Growth Index (the "Index") in the same period. For the trailing 12-month period, the Portfolio returned 12.85% gross of fees compared to -0.47% for the Index.

In the second quarter of 2019, global markets continued higher after the strong rebound in the first quarter. Periods of volatility were tied to headlines about trade and more accommodating monetary policy from central banks. U.S. economic reports remained mostly strong and broad inflation measures remain subdued. Two macro factors that many of our portfolio companies face are wage inflation for service-related jobs and tariffs. We believe our holdings are managing these risks well and that they will not materially affect cash flows for the Portfolio in aggregate.

Our companies continue to perform well, exhibiting above-average growth rates, high returns on invested capital, and low levels of financial leverage. On a trailing 12-month basis, the weighted average sales growth in our portfolio was just over 19% with strong conversion to earnings and free cash flow. For the same time period, weighted average return on invested capital was nearly 17% and cash-based returns were even higher. Our total debt to total capital on a weighted-average basis was just under 21%, reflecting prudent balance sheet management. Just as important in our view, we think the management teams of our portfolio companies continue to make capital stewardship decisions to drive future growth with high returns on capital. These portfolio metrics build our confidence in the long-term sustainability of the companies we own, and they compare favorably with the benchmark.

Before reviewing quarterly performance, we encourage our investors to review our longer-term results which we believe better align with our long-term orientation. Periods of high volatility can make evaluating short-term performance difficult. Reflecting upon the last twelve months, market volatility has been particularly acute with a large sentiment-driven drawdown in the fourth quarter of 2018, and, in the last six months, a rebound that pushed the markets to new highs.

Portfolio Performance & Activity

Performance this quarter was driven entirely by stock selection, especially in the technology and healthcare sectors, and by some of our largest holdings including Globant, Fox Factory, and Pool Corporation. Gains were partially offset by weakness in a single stock, Stamps.com, which we detail later in this letter.

During the quarter, the total impact from sector allocation was negligible. Relative performance by sector was largely driven by security selection rather than allocation. Our underweight to industrials, the strongest performing sector in the benchmark, was offset by our underweight to sectors that lagged the index, including healthcare, communications services, and energy. The sectors that showed the best relative returns were technology and healthcare. Within technology, Globant and Paycom were standouts. In healthcare, results were helped by the acquisition of Medidata and the rebound of several holdings that had come under pressure in past periods. Specifically, Cantel Medical and AMN Healthcare were positive contributors after a couple of quarters of underperformance due to mixed results in parts of their businesses. No other sector materially detracted from performance, apart from industrials, and despite our underweight to that sector, our stock selection within it was positive.

In terms of factor-driven performance, our style of high-quality growth investing was not a meaningful contributor to small-cap stock performance during the quarter, and performance was relatively balanced across ROIC quintiles. This is a reversal from the first quarter when the lowest ROIC companies were the strongest contributors. In terms of growth, like last quarter, the fastest growers performed the best. Our overweight to and stock selection within the second highest sales growth quintile helped performance and more than offset the negative allocation effect from being underweight the highest sales growth companies in the Index. As a reminder, it is our intent to own companies that we believe can sustainably grow their sales while also expanding earnings, cash flow and returns. We typically find that the companies in the top sales growth quintile are not generating profits and have stretched balance sheets. We question the sustainability of these companies, and we are typically underweight this quintile.

Our largest contributors in the quarter showed relative price strength due to a combination of stronger-than-expected growth, margin expansion, idiosyncratic factors, and M&A. The top contributors are listed in order of magnitude of impact on the Portfolio.

Globant SA was our strongest contributor with the stock price increasing nearly 42% in the quarter. The company continues to report excellent results, exceeding management's long-term revenue growth targets. The biggest drivers of this strength are robust global demand for digital transformation and successful penetration of the firm's existing account base through cross selling. We continue to believe Globant is well-positioned in the fast-growing digital strategy consulting services industry as companies across all industries have an ongoing need to strengthen their online presence, better leverage technology in their own products and services, and drive customer experience. We have confidence in Globant's ability to continue to grow revenues 20%+ annually by leveraging its brand, excellent customer relationships, deep digital expertise, and scale. We believe this top-line growth should convert to even better EPS and cash flow growth as the company delivers more revenue per professional and leverages its SG&A investments.

Fox Factory Holding Corporation was our second largest contributor with the stock increasing 18% in the quarter. As a manufacturer of high quality ride dynamics products, Fox Factory continues to exceed growth expectations. We are impressed with the performance of its Powered Vehicles segment where it is having considerable success selling off-road automotive suspension products and gaining traction with OEM's. In our view, the firm's successful expansion to off-road vehicles demonstrates Fox Factory's competitively advantaged brand and reputation and its management's ability to successfully expand into large adjacent categories. We believe the company can continue to increase market share in all its end markets due to the high quality of its products and its skilled management team.

Pool Corporation was a strong contributor with the stock price increasing 16% in the quarter. Business is actually off to a slower-than-expected start this year due to weather challenges. We believe the market responded favorably despite slower sales growth in the short-term because of the company's strong cost controls in the quarter. This demonstrates Pool's resilient profit model and management's exceptional execution. The company remains the leading distributor in what we believe to be a very healthy and resilient market that is tied to non-discretionary pool maintenance and repair.

We continue to have confidence in the company's ability to drive 6-8% organic sales growth and mid-teens incremental margins over the long-term.

Medidata Solutions Inc. was also a top contributor in the quarter, up nearly 24%. Early in the quarter, rumors surfaced that the company was going to be acquired by Dassault Systemes. The stock reacted favorably to the news before an all-cash deal at $92.50 per share was officially announced in June. The acquisition price represents a roughly 17% premium prior to the transaction rumors. The deal is expected to close in the fourth quarter of 2019. We intend to sell the position when we find a good replacement.

Our largest detractors in the quarter showed relative price weakness largely due to idiosyncratic factors.

Stamps.com was our largest detractor, down 51% in the quarter. This was the second consecutive quarter of poor performance for the firm. During the quarter, the company made a disappointing announcement detailing the negative effects of USPS renegotiating terms with Stamps.com's affiliate partners, which would substantially reduce Stamps.com's profitability. The announcement came on the heels of last quarter's announcement that Stamps.com would be ending its own exclusive partnership with the USPS—the firm is seeking to better position itself to partner with other shipping companies that offer more compelling shipping solutions. The substantial impact of the affiliate relationships on profitability came as a surprise to us and most investors. We decided to exit the position, which we detail later in this letter.

Alarm.com was our next largest detractor, down nearly 18% in the quarter. The company reported strong results and we believe continues to be well-positioned to execute against its long-term plans. We believe the weakness in the stock was related to two issues. First, the core Alarm.com subscription growth rate decelerated, although it is still strong at nearly 20%. Second, the impact from Chinese tariffs on the company's hardware products, 1/3 of which are sourced from China, spurred investors' worries. We do not believe either issue should be concerning for long-term investors. Alarm.com continues to have an attractive business model with strong recurring revenue growth, high customer renewal rates, and solid margins with room for additional operating leverage. Additionally, management continues to prudently deploy capital in areas that enhance the firm's long-term market opportunity.

Inogen, Inc. was the next largest detractor, down 30% in the second quarter after a weak first quarter. The company continues to report mixed results. The firm has experienced a decline in orders from a large business-to-business customer and a slower-then-expected ramp in its new direct-to-consumer facility. While we think these two issues are temporary, we are concerned by the company's weak execution following management's decision to heavily invest in its direct-to-consumer expansion efforts. We think Inogen is making the right choices given the high incidence of chronic obstructive pulmonary disorder, low penetration of portable oxygen concentrators and the recent changes in Medicare reimbursement. However, we have been surprised by the slower-than-expected revenue growth, low sales rep productivity, and higher-than-expected expenses. We continue to evaluate whether we believe this strategic shift is a good long-term decision and aim to better understand why early execution is weak.

Texas Roadhouse was also a detractor, down 13% in the quarter. The company reported first quarter results that showed strong comparable store sales growth of 5% but weaker restaurant margins driven by rising labor and food costs. Management also highlighted that comparable store sales, while very high in January, slowed throughout the first quarter and into April. That said, it is not unusual for comparable store sales to fluctuate quarter to quarter. Regarding inflation, we do not believe the company's labor and commodity cost-related problems are insurmountable. Management's pricing philosophy has always been conservative, and the restaurant's menu prices remain low relative to competitors. We believe the firm can offset some of the inflation by raising prices more aggressively, which we expect to see later this year. As we look out longer term, we are closely monitoring most the runway for the company's core Texas Roadhouse concept. The results at Bubba's, the company's newer concept, have been mixed. We think this company is well run and we will continue to watch these issues evolve and analyze the firm's viability as a long-term holding in the Portfolio.

There were several changes to the Portfolio during the quarter.

We started a new position in **U.S. Physical Therapy**, a "watch list" company for over a year. U.S. Physical Therapy (USPH) is a leading provider of outpatient physical therapy services and the third largest operator in the U.S. with roughly 4% market share. The outpatient physical therapy industry is attractive and has grown at a mid-single digit rate due to structural tailwinds, like favorable demographics and shift to lower cost providers, that we believe will persist. The company has a highly skilled, long-tenured management team with a unique acquisition strategy that has created value over many years—it seeks to acquire and retain owners of single and multi-clinic practices nationwide. USPH's Clinic Partnership model affords numerous advantages to both management and therapists including an ownership stake, outsourcing administrative burdens, and scale benefits. This arrangement retains the therapist's relationships with patients and referring physicians. This combination creates a capital-lite business that generates significant cash flow. We believe the model is repeatable for the foreseeable future in what is still a very fragmented industry where no single player has greater than 10% market share.

We sold our position in **Healthcare Services Group**, the leading provider of laundry and dining services to long term care facilities such as nursing homes, retirement complexes, rehabilitation centers, and hospitals. We liked the company for its long history of solid revenue growth, long-term contracts that were recurring in nature, and consistently high returns on capital despite an end market that experiences regulatory and liquidity challenges from time to time. In our view, management has shown tremendous skill over the years in delivering attractive cost savings to its customers who are continuously pressured by rising costs and payor cuts. However, the company has struggled over the last year with slower growth and lower cash generation due to a spike in bankruptcies among customers. While its customers' issues are cyclical, they appear to us to be worse this cycle and the duration is uncertain. Late last year, management signaled the firm was through the worst of the cycle after several quarters of improvement. When fundamentals deteriorated again in the first quarter of this year, it became more difficult to discern the cycle's duration. We are concerned with the company's increased exposure to larger customers, which tend to be the most at risk due to high leverage. The company's large exposure to Genesis, a customer which is highly levered and currently going through a restructuring, adds to our concerns. After reevaluating the business, we felt we had more attractive investments within our existing portfolio and in our research pipeline with better risk-reward dynamics and a more certain outlook. We decided to sell Health Care Services Group and buy U.S. Physical Therapy.

We sold our position in **Stamps.com** after a disappointing string of announcements, an end to its exclusive USPS partnership and USPS's renegotiated terms with Stamps.com affiliates, led to considerable value erosion. Our investment case and assumptions hinged on the company using the cash flow it generated from its mutually beneficial relationship with the USPS to diversify the business via acquisitions into a more broad-based multi-carrier provider of shipping services. Since 2014, management deployed more than $500 million of internally generated cash flows to expand its presence into these multi-carrier solutions. As the company integrated acquisitions, all the customer metrics were trending well, churn was low and the returns on capital were attractive.

However, new information from the latest announcement revealed that the company had been generating its high returns in a way that was inconsistent with our understanding. In turn, we realized that the affiliate relationships generated substantially more profit than we originally assumed, and the remaining multi-carrier business had worse economics than we originally believed. We were also surprised to learn that despite what management reported to investors, the company had been increasing exposure to the USPS rather than diversifying the business. For us, this reflects poor management judgement, poor capital stewardship, and a lack of transparency. We consider these major violations of our flywheel philosophy and our standards for investment.

A permanent loss of capital event like this is a disappointing result and something that we always strive to avoid. We will use this reference case to keep learning and pushing to ask more of the right questions and make sure we challenge our assumptions. We believe that this is one of our competitive strengths, and we will use this situation to improve in the future.

Outlook

We believe the fundamental growth prospects for the companies in our Portfolio remain attractive. Most importantly, we feel the companies in our Portfolio should hold up across macro-economic or capital cycles. Our portfolio companies are self-funding and well-positioned to strengthen their competitive position in the event of an economic downturn. We are now more than ten years removed from the global financial crisis with an unprecedented period of extremely low interest rates. Even after the Federal Reserve increased rates over the last few years, rates continue to be very low by historical standards. Accommodative monetary policy encourages risk-taking across all asset classes. Persistently low interest rates have encouraged many companies to grow as fast as possible without regard for profit or positive cash flow. We have referenced the high percentage of loss-making companies in our universe before and remain cautious about the prospects for many of these companies. We favor companies that generate cash and high returns on capital and believe that protection of capital and long-term compounding comes from owning profitable, high-quality businesses. As portfolio managers, we have seen periods of extreme volatility and appreciate how important it is to own the best businesses that have the financial flexibility to keep a long-term focus even when the economy is weak. Given the length of the cycle and increasing global macro risks, we believe it is more important than ever to own high quality businesses.

As we look across the landscape to find new investments in the small-cap universe, we continue to be discerning. Our process targets real organic revenue growth, a strong margin structure, positive free cash flow, high returns on capital, and manageable amounts of leverage, if any. If a company meets our quality standards, we wait for what we believe is a fair price that gives us a good chance at achieving our 15% IRR hurdle over five years. We are constantly searching for high-quality investments, and we look forward to discussing these opportunities in future letters.

Team Update

We are thrilled to announce a new addition to the team. Shane Smith just joined us as an Analyst, providing research for both Small Company Growth strategies. Prior to joining our team, Shane was an equity analyst at Franklin Templeton, focused on global small caps. Shane has been analyzing businesses around the globe for a high-quality strategy and his experience and commitment to continuous learning are a great fit for our team. This now brings the team to six members, three of which are dedicated analysts. Our strong process orientation has made it easy for the analysts to become instant contributors to the research and decision-making processes. We will continue to evaluate our needs on an ongoing basis and selectively add talented people that fit with our culture and bring diversity of thought to ensure consistent execution of our process and seek the best outcomes for our shareholders.

We appreciate the opportunity to manage your assets in this category. We look forward to speaking with you soon.

Sincerely,

Tucker Walsh & Rayna Lesser Hannaway

Historical Performance

US Small Company Growth SMA Composite as of Jun-30-2019			
	Polen (Gross)	**Polen (Net)**	**R2000G**
Jun-19	6.96	6.96	7.70
3 Month	6.56	6.33	2.75
YTD	22.13	21.59	20.37
1 Year	12.85	11.81	-0.47
Since Inception (3/9/17)	20.00	18.87	11.69

Returns are trailing through June-30-2019

Annualized returns are presented for periods greater than 1 year.

Source: Archer

GIPS Disclosure

Polen Capital Management

U.S. Small Company Growth Composite - Annual Disclosure Presentation

		UMA	Firm	Composite Assets		Annual Performance Results				3 Year Standard Deviation	
Year End	Total (millions)	Assets (millions)	Assets (millions)	U.S. Dollars (millions)	Number of Accounts	Composite Gross	Composite Net	Russell 2000 Growth	Composite Dispersion	Polen Gross	Russell 2000 Growth
2018	20,591	7,862	12,729	3.82	6	3.30%	2.31%	-9.29%	0.1	-	16.7
2017*	17,422	6,957	10,466	5.65	4	20.74%	19.82%	17.33%	N/A	-	14.8

Note: N/A - There are five or fewer accounts in the composite the entire year.

Total assets and UMA assets are supplemental information to the Annual Disclosure Presentation.
**Performance represents partial period (March 9, 2017 through December 31, 2017), assets and accounts are as of December 31, 2017.*

GIPS Disclosure

The U.S. Small Company Growth Composite created on March 9, 2017 contains fully discretionary small company equity accounts that are not managed within a wrap fee structure and for comparison purposes is measured against Russell 2000 Growth. Polen Capital invests exclusively in a portfolio of high-quality companies.

Polen Capital Management claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Polen Capital Management has been independently verified by ACA Performance Services, LLC for the periods January 1, 2016 through June 30, 2018. A verification covering the periods from April 1, 1992 through December 31, 2015 was performed by Ashland Partners & Company LLP, which was acquired by ACA Performance Services, LLC, whose report expressed an unqualified opinion thereon.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

Polen Capital Management is an independent registered investment adviser. The firm maintains a complete list and description of composites, which is available upon request. In July 2007, the firm was reorganized from an S-corporation into an LLC and changed names from Polen Capital Management, Inc. to Polen Capital Management, LLC.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. Effective January 1, 2018, accounts must be fully invested at the market open on the first business day of the month, in order to be included in that month's composite.

The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of fees and include the reinvestment of all income. Net of fee performance was calculated using actual fees. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The management fee schedule is as follows:
Institutional: Per annum fees for managing accounts are 100 basis points (1.00%) on the first $50 Million and 85 basis points (0.85%) on all assets above $50 Million of assets under management. HNW: Per annum fees for managing accounts are 175 basis points (1.75%) of the first $500,000 of assets under management and 125 basis points (1.25%) of amounts above $500,000 of assets under management. Actual investment advisory fees incurred by clients may vary.

Past performance does not guarantee future results and future accuracy and profitable results cannot be guaranteed. Performance figures are presented gross and net of fees and have been calculated after the deduction of all transaction costs and commissions. Polen Capital is an SEC registered investment advisor and its investment advisory fees are described in its Form ADV Part 2A. The advisory fees will reduce clients' returns. The chart below depicts the effect of a 1% management fee on the growth of one dollar over a 10 year period at 10% (9% after fees) and 20% (19% after fees) assumed rates of return.

The Russell 2000® Growth Index measures the performance of those Russell 2000 companies with higher price/book ratios and higher forecasted growth values.

The information provided in this document should not be construed as a recommendation to purchase or sell any particular security. There is no assurance that any securities discussed herein will remain in the composite or that the securities sold will not be repurchased. The securities discussed do not represent the composite's entire portfolio. Actual holdings will vary depending on the size of the account, cash flows, and restrictions. It should not be assumed that any of the securities transactions or holdings discussed will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein. A complete list of our past specific recommendations for the last year is available upon request.

Return	1 Year	2 Years	3 Years	4 Years	5 Years	6 Years	7 Years	8 Years	9 Years	10 Years
10%	1.1	1.21	1.33	1.46	1.61	1.71	1.95	2.14	2.36	2.59
9%	1.09	1.19	1.3	1.41	1.54	1.68	1.83	1.99	2.17	2.39
20%	1.2	1.44	1.73	2.07	2.49	2.99	3.58	4.3	5.16	6.19
19%	1.19	1.42	1.69	2.01	2.39	2.84	3.38	4.02	4.79	5.69