AMI
ASSET MANAGEMENT

*"I frequently hear music in the very heart of noise." – George Gershwin*

**Third Quarter 2018**

Equities climbed higher during Q3, with the S&P 500 up 7.71% for the quarter. Investors showed an ability to tune out noise and focus on economic fundamentals, showing resilience in the face of ongoing political and trade uncertainty. Interestingly, the S&P didn't close up or down more than 1% on a single trading day during Q3, only the second time that has happened in what is a historically volatile quarter (1963 was the only other instance). The lack of volatility in Q3 is in sharp contrast to how Q4 has begun.

There were interesting rotations in market leadership throughout the quarter. For much of the year, technology stocks comprised a large percentage of the gains in the S&P 500. However, after weak earnings from Netflix and a disappointing outlook from Facebook, defensive stocks, which had been widely sold in the first half of the year, led the market higher in July. Technology did recapture its leadership role in mid-August, only to reverse yet again in September.

The initial round of tariffs on $50 billion of Chinese goods was enacted in early July, followed by the proposal of an additional $200 billion in August. The ongoing conflict with China, and the likelihood of a slowdown in Chinese economic growth led to a pronounced selloff in emerging markets currencies. Diplomatic conflict with Turkey and fiscal issues in Argentina and Italy exacerbated the broader selloff. Trade with China, and any progress or deterioration of those negotiations, will be in focus through the end of the year. That said, the Trump Administration has a track record of elevated rhetoric, followed by effective negotiations (e.g. the recent reworking of the former NAFTA deal), and the strong performance in U.S. equities during Q3 indicates the market expects a similar outcome.

A strong Q2 earnings season helped investors move past trade rhetoric, and most economic data remained healthy throughout the quarter. In Q2, GDP growth of 4.2% was the strongest since 2014, with consumer spending leading the way. In contrast, the housing market was impacted by higher interest rates and elevated prices throughout the summer. Housing is widely viewed as a leading economic indicator; however the problems in the housing market seem driven by strong demand and a lack of inventory, an indication of economic strength, and less so by the issues that plagued housing and the broader economy at the end of last decade.

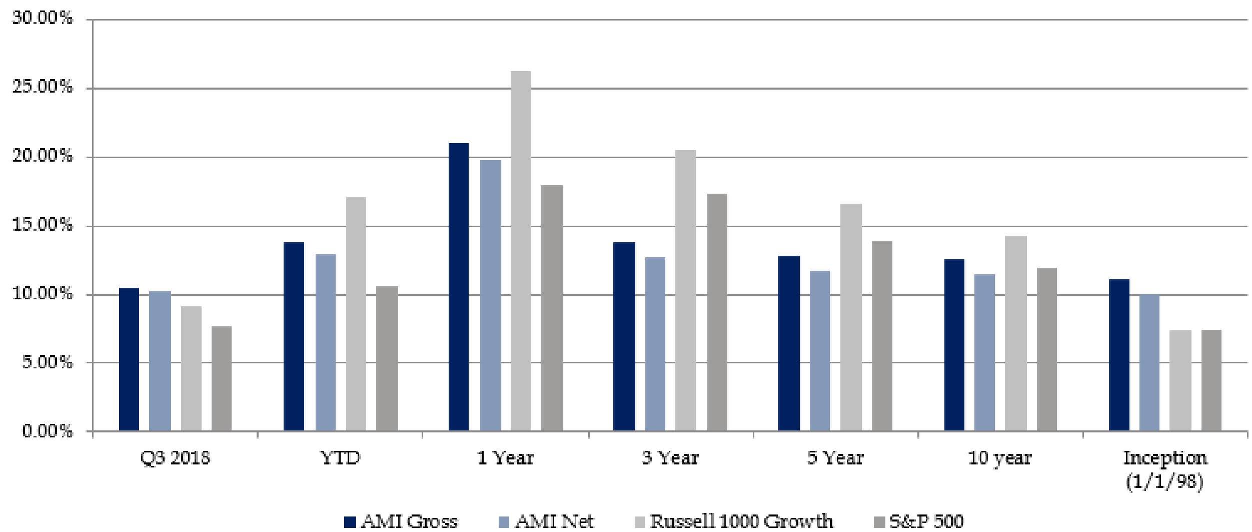
While the September jobs report came in below expectations (134K vs. 185K estimate), largely due to disruptions from Hurricane Florence, both July and August were revised strongly higher, and wage gains remained strong at +2.8% year-over-year. After increasing the Fed Funds target range by 25 bps to 2.00 – 2.25% in September, the Fed looks set to continue its tightening cycle through the end of the year. While monetary tightening reflects a strong economy, rapidly rising intertest rates present a threat to the ten-year bull market in equities. As a reminder, AMI seeks to own high quality companies with defensible business models that we believe will perform well in up as well as down markets.

**AMI Large Cap Growth Strategy**

In Q3, the AMI Large Cap Growth strategy outperformed the Russell 1000 Growth index by 1.32% on a gross basis (1.07% on a net basis). This outperformance was driven entirely by security selection, with allocation a negative contributor to performance. Outperforming stock picks in Consumer Staples, Technology and Consumer Discretionary were partially offset by underperforming picks in Producer Durables and Healthcare. Being overweight Consumer Staples and Energy (which underperformed the index) was partially offset by being overweight Healthcare (which outperformed).

## LARGE CAP GROWTH ANNUALIZED RETURNS

*Growth Through Stability*




| | Q3 2018* | YTD* | 1 Year | 3 Year | 5 Year | 10 year | Inception (1/1/98) |
|---|---|---|---|---|---|---|---|
| **AMI Gross** | **10.49%** | **13.79%** | **20.95%** | **13.76%** | **12.78%** | **12.54%** | **11.09%** |
| **AMI Net** | **10.24%** | **12.98%** | **19.80%** | **12.66%** | **11.69%** | **11.45%** | **10.01%** |
| Russell 1000 Growth | 9.17% | 17.09% | 26.30% | 20.55% | 16.58% | 14.31% | 7.43% |
| S&P 500 | 7.71% | 10.56% | 17.91% | 17.31% | 13.95% | 11.97% | 7.44% |

*Not annualized. As of 9/30/18. Net returns are based on the highest annual fee paid by AMI clients of 1.00%. The annual fee schedule for institutional accounts is as follows: 0.70% for the first $10 million, 0.60% on the next $15 million, 0.50% on the next $25 million and 0.40% on the balance. The above information is based on the Domestic Large Cap Growth Composite and clients accounts may vary and includes the reinvestment of dividends and other earnings. Past performance is not an indication of future returns. Please refer to important disclosures on last page. Source – AMI.

As seen in the table below, the top contributors to Q3 performance were Apple, West Pharmaceutical Services, Church & Dwight, Mastercard and Biogen. The bottom contributors to Q3 performance were PepsiCo, Diamondback Energy, Charles Schwab, Healthcare Services Group and Laboratory Corp. of America.

**Top Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| Apple | 3.99% | 22.38% | 0.84% |
| West Pharmaceutical Services | 2.81% | 24.53% | 0.64% |
| Church & Dwight | 4.84% | 12.12% | 0.59% |
| Mastercard | 4.06% | 13.42% | 0.56% |
| Biogen | 2.58% | 21.73% | 0.52% |

**Bottom Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| PepsiCo | 3.37% | 3.53% | 0.13% |
| Diamondback Energy | 1.55% | 2.86% | 0.04% |
| Schwab | 3.15% | -3.57% | -0.12% |
| Healthcare Services Group | 1.96% | -5.51% | -0.12% |
| LabCorp | 3.76% | -3.26% | -0.13% |

## Top Contributors

**Apple (AAPL)** - Apple posted a very strong fiscal Q3 as services growth remained robust (up 31% year-over-year) and is now becoming a meaningful growth driver. Customers gravitated toward higher-priced iPhone models, boosting revenues in Apple's largest product category. Apple's Other Products category (AirPods and the Apple Watch) grew an impressive 37% year-over-year. The company remains confident in its activity in China and other international markets which were all up double digits as compared to the year-ago period.

**Church & Dwight (CHD)** - Church & Dwight continued to post results that outpaced the broader household and personal care industry in Q2. Church's ability to drive value-added innovation in its key segments has driven industry-leading volume growth, with a positive contribution from the recently acquired WaterPik business. Church's high-quality brands, asset-lite manufacturing and nimble corporate structure should continue to drive ongoing outperformance.

**West Pharmaceutical Services (WST)** - West Pharmaceutical Services reported strong quarterly results as the supplier of drug vial and syringe components is experiencing stabilized order patterns following a period of customer inventory reductions. After a period of capacity constraints, West expanded manufacturing to meet demand and customers reduced their inventory levels to coincide with shorter lead times. These reductions weighed on revenue during 2017 and into 2018 but have since improved. The growth outlook appears solid as West's products are integral components to many new drugs coming to market, especially in the faster growing biologics market.

**Mastercard (MA)** - Mastercard reported another solid quarter with sales and adjusted EPS growth of 20% and 51%, respectively. As developed economies grow GDP and emerging economies shift from cash to electronic payments, Mastercard is benefitting from increased use of debit/credit cards. The tax reform act and stock buybacks are also helping drive EPS growth.

**Biogen (BIIB)** - Biogen stock rose early in Q3 following the announcement of positive phase 2 data from Eisai, its partner in an Alzheimer's disease treatment called BAN-2401. Biogen and Eisai are partnered on several Alzheimer's treatments and, given that BAN-2401 is similar to a drug that is farther along in phase 3 trials, investors increased their assessment of the likelihood of success. Biogen is currently one of the companies with the most advanced treatment and if successful it could represent a sizable opportunity.

**<u>Bottom Contributors</u>**

**PepsiCo (PEP)** - Pepsi reported sequential improvement in the North American Beverages business in Q2, which had underperformed for most of the past year. Pepsi's relatively weak stock performance this quarter was largely related to the announced retirement of longtime CEO Indra Nooyi, who has reshaped the company's portfolio to focus on higher growing better-for-you brands. While any management change brings uncertainty, we continue to like Pepsi's beverage and snack brands and believe the company is poised for strong growth moving forward.

**Diamondback Energy (FANG)** - In conjunction with strong quarterly results reported in early August, Diamondback Energy announced the acquisition of Ajax Resources and shortly thereafter the all-stock acquisition of Energen. While both deals are attractive in terms of the assets acquired, Diamondback's stock initially traded lower driven by the share issuance to finance the transactions and some investor skepticism surrounding management's anticipated synergies for the Energen deal. We like Diamondback and expect the company to continue self-funding production growth while achieving cost and production synergies from the recent acquisitions.

**Charles Schwab (SCHW)** - Schwab reported a very good second quarter with 17% revenue and 53% EPS growth. However, fee pressure due to growth in lower margin ETFs and higher forecasted expenses in Q3 weighed on the stock. Nevertheless, we expect Schwab to continue its strong pace of asset gathering while also benefiting from higher interest rates.

**Healthcare Services Group (HCSG)** - Healthcare Services Group reported disappointing Q2 results as gross margins declined slightly following improvement from a low in Q3 of last year. However, management remains confident in their gross margin target for FY 18 and is focused on building its manager pipeline following large new business adds last year. We believe Healthcare Services Group is best positioned to capitalize on the large and underpenetrated opportunity for housekeeping and dining services outsourcing at long-term care facilities.

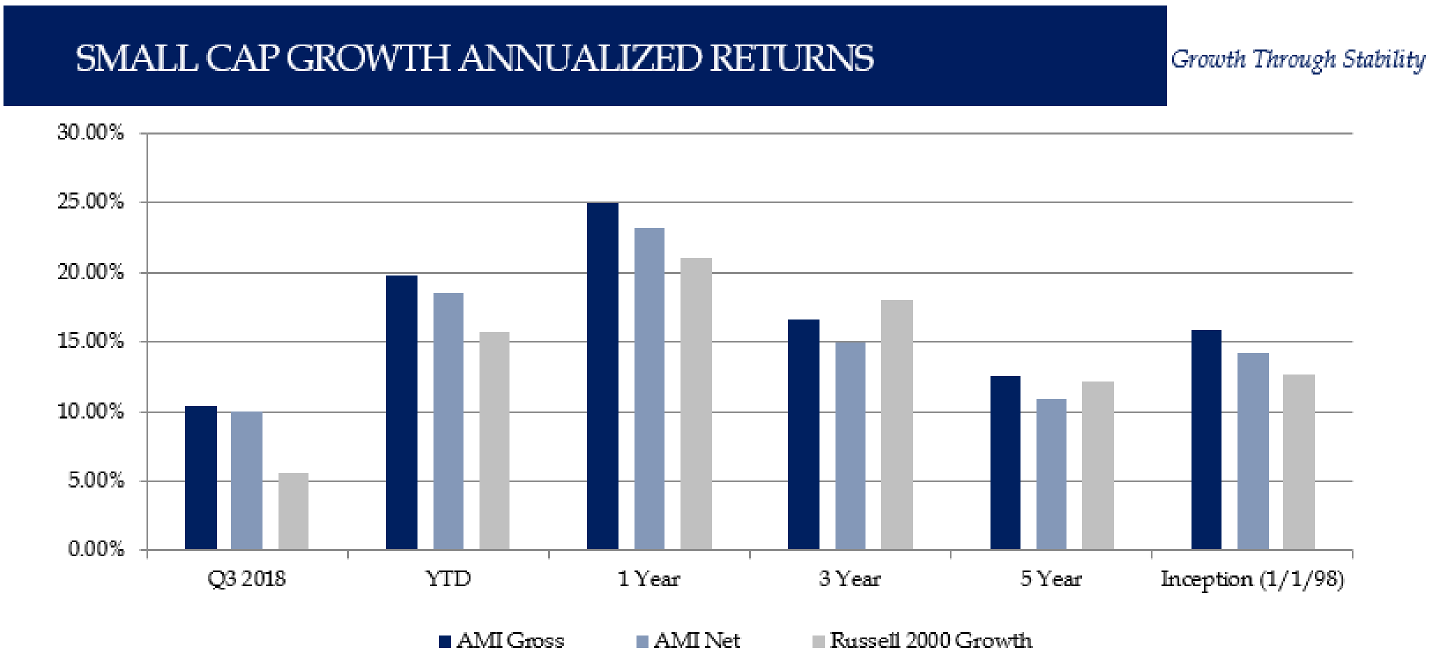
**LabCorp (LH)** - LabCorp reported inline Q2 results but failed to exceed elevated expectations. In addition, the company will see some EPS pressure from the recently renewed agreement with UnitedHealth that will now be shared with top competitor Quest Diagnostics. This new agreement removes the risk that the large contract could have been lost completely but it was not as attractive as an exclusive relationship. Nevertheless, we view this outcome as positive and we remain bullish on LabCorp.

## Portfolio Additions and Deletions

There were no portfolio additions or deletions during Q3.

## AMI Small Cap Growth Strategy

The AMI Small Cap Growth strategy outperformed the Russell 2000 Growth index in Q3 by 4.93% on a gross basis (4.56% on a net basis). The outperformance was driven almost entirely by security selection. Outperforming stock picks in Healthcare, Financial Services and Consumer Discretionary were partially offset by underperforming picks in Producer Durables and Technology. Asset allocation had a slightly positive contribution to performance, as a result of being underweight Materials (which underperformed the market), partially offset by being overweight Consumer Staples (which underperformed the market).




| | Q3 2018* | YTD* | 1 Year | 3 Year | 5 Year | Inception (10/1/08) |
|---|---|---|---|---|---|---|
| **AMI Gross** | **10.45%** | **19.78%** | **25.01%** | **16.68%** | **12.52%** | **15.86%** |
| **AMI Net** | **10.08%** | **18.52%** | **23.24%** | **15.00%** | **10.89%** | **14.19%** |
| Russell 2000 Growth | 5.52% | 15.76% | 21.07% | 17.98% | 12.14% | 12.65% |

*Not annualized. As of 9/30/18. Net returns are based on the highest annual fee paid by AMI clients of 1.50%. The annual fee schedule for institutional accounts is as follows: 0.90% for the first $10 million, 0.80% on the next $15 million, 0.70% on the next $25 million and 0.60% on the balance. The above information is based on the Domestic Small Cap Growth Composite and clients accounts may vary and includes the reinvestment of dividends and other earnings. Past performance is not an indication of future returns. Please refer to important disclosures on last page. Source – AMI.

As seen in the table below, the top contributors to Q3 performance were PetIQ, Ligand Pharmaceuticals, Dave & Buster's, Anika Therapeutics and The Simply Good Foods Company. The bottom contributors to Q3 performance were SiteOne Landscape Supply, MGP Ingredients, LogMeIn Inc., Performance Food Group and Innerworkings Inc.

**Top Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| PetIQ | 3.45% | 46.35% | 1.43% |
| Ligand Pharmaceuticals | 4.02% | 32.50% | 1.22% |
| Dave & Buster's | 3.03% | 39.44% | 1.10% |
| Anika Therapeutics | 3.10% | 31.81% | 0.86% |
| Simply Good Foods | 2.74% | 34.70% | 0.84% |

**Bottom Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| SiteOne Landscape Supply | 3.09% | -10.28% | -0.30% |
| MGP Ingredients | 2.36% | -10.94% | -0.31% |
| LogMeIn Inc. | 2.52% | -13.39% | -0.34% |
| Performance Food Group | 3.37% | -9.26% | -0.34% |
| Innerworkings | 0.87% | -17.26% | -0.51% |

## Top Contributors

**PetIQ (PetQ)** - PetIQ reported strong second quarter results, as the company's business of distributing veterinary medications into traditional retail pharmacies is firing on all cylinders. Combined with the ongoing rollout of the company's VetIQ clinics in Walmart and other retailers, the growth opportunities remain very robust. We expect PetIQ to continue to post strong revenue and earnings growth for the foreseeable future.

**Ligand Pharmaceuticals (LGND)** -Ligand Pharmaceuticals reported another strong quarter driven by patient growth and indication expansion in the two main royalty generating drugs (Kyprolis from Amgen and Promacta from Novartis). The stock also rose on continued progression of the pipeline, including several large potential opportunities over the next several years.

**Dave & Buster's (PLAY)** -Following a challenging start to the year, Dave & Buster's has returned to solid growth, driven by a proprietary virtual reality (VR) game and improved food and beverage offerings. The company continues to open new stores with strong returns on investment. We believe that Dave & Buster's strong margins and traffic growth driven by additional VR games will lead to continued success.

**Anika Therapeutics (ANIK)** - Late in Q2, Anika's stock fell substantially after it announced that its next generation osteoarthritis treatment, Cingal, failed to provide a benefit over steroids. However, the stock recovered in Q3 after a better-than-expected earnings report and management commentary that it was committed to bringing this product to market. We expect to see final results of the trial late in 2018, which may ultimately show a benefit and thus we remain bullish on the name.

**Simply Good Foods Company (SMPL)** -Simply Good Foods reported strong results in the company's fiscal third quarter, with impressive double-digit revenue growth in what has been a generally challenging environment for packaged food. The company continues to benefit from a broader consumer shift to better-for-you, low carb snacking, with additional momentum driven by a new national marketing campaign. With plenty of distribution opportunities and the prospect of accretive M&A, we continue to like the stock.

**Bottom Contributors**

**SiteOne Landscape Supply (SITE)** - SiteOne underperformed due to weakness in the new home construction, where the company's landscape distribution business has some exposure. However, the majority of SiteOne's revenues are tied to the recurring maintenance business, which is core to our bullish thesis. We remain positive on SiteOne as the company's position as a consolidator in a highly fragmented market should drive strong revenue and earnings growth over the long term.

**MGP Ingredients (MGPI)** - MGP Ingredients reported second quarter earnings that were below expectations, driven by timing issues in shipments of aged whiskey to customers. In addition, the potential impact of retaliatory tariffs on bourbon (especially in the EU, a large export market) hurt sentiment on bourbon companies. However, the majority of MGP's customers are based in the United States, with the likelihood of any impact from tariffs negligible. MGP's markets continue to grow nicely, with many startups launching new brands every year. MGP should be able to grow earnings in the high-teens over the next few years as it supports customers with its inventory of aged whiskey, while also building its own brands.

**LogMeIn (LOGM)** - LogMeIn Q2 revenue and EPS beat estimates but the company guided full-year results lower due to weakness in its core Collaboration business. When the company acquired the GoToMeeting assets, it began to implement new business practices with respect to pricing and renewals. While the intent was to drive overall revenue higher, the changes created some friction in the renewal process and LogMeIn's competition took advantage by offering various incentives to switch. Management believes it has identified the issues within its customer base and has implemented remedies. We believe that the shares are undervalued given the strength in its other businesses as well as the potential for improvement in Collaboration.

**Performance Food Group (PFGC)** -Performance Food Group reported mixed fiscal Q3 earnings, with solid revenue and volume growth offset by higher operating costs. These higher costs were driven by a shortage of drivers, as well ongoing investments to build out the company's salesforce. Performance Food has gone through these types of investment cycles in the past, and the long-term revenue growth benefits outweigh the temporary contraction in profitability. We believe the company is well positioned to continue to grow volume with independent restaurants over the long term and we also like the diverse customer set (movie theaters, e-commerce, dollar stores) of Performance Food's Vistar subsidiary.

**Innerworkings (INWK)** - In July, Innerworkings reported Q1 results that missed estimates driven by significant reductions in marketing spend at one of the company's largest clients. As a result, margins were pressured and management announced a cost reduction and business improvement plan. We saw significantly elevated execution risk following the announcement and decided to exit our position.

## Portfolio Additions and Deletions

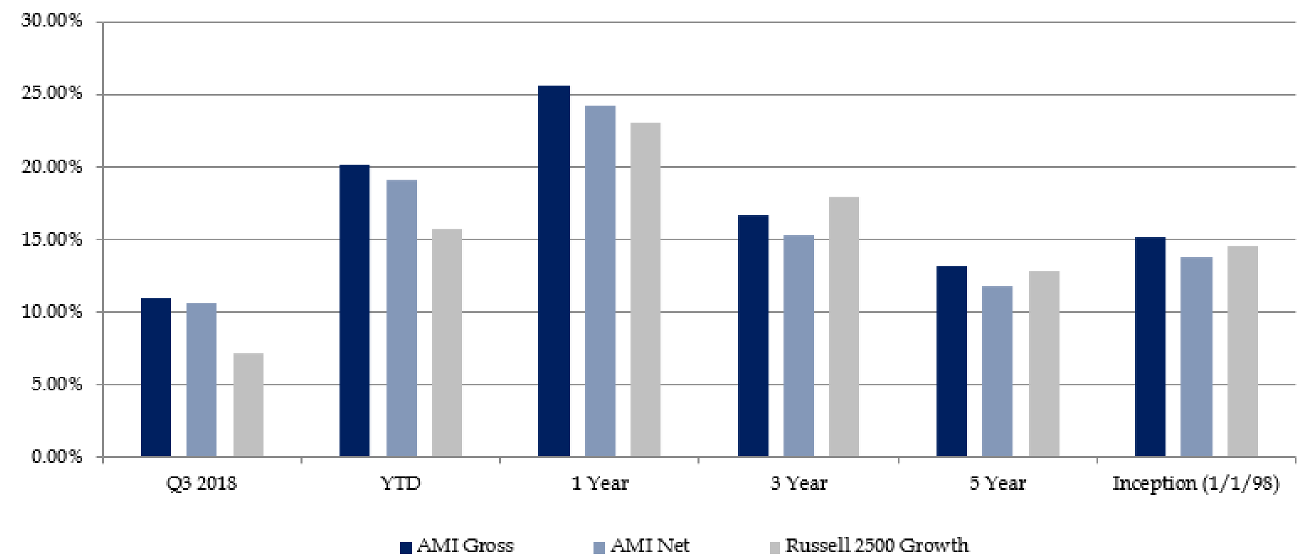
There were no portfolio additions during Q3. As noted above, we sold Innerworkings.

## AMI SMID Cap Growth Strategy

In Q3, the AMI SMID Cap Growth strategy outperformed the Russell 2500 Growth index by 3.80% on a gross basis (3.49% on a net basis). The outperformance was driven by stock selection, with asset allocation a slightly negative contribution to performance. Outperforming stock picks in Health Care, Financial Services and Consumer Discretionary were partially offset by underperforming stock picks in Producer Durables and Technology. Asset allocation negatively impacted performance as a result of being underweight Technology (which outperformed the market) and being overweight Consumer Staples (which underperformed), with a partial offset from being underweight Materials and Consumer Discretionary (which underperformed the market).

### SMID CAP GROWTH ANNUALIZED RETURNS

*Growth Through Stability*




| | Q3 2018* | YTD* | 1 Year | 3 Year | 5 Year | Inception (4/1/13) |
|---|---|---|---|---|---|---|
| **AMI Gross** | **10.97%** | **20.18%** | **25.70%** | **16.72%** | **13.17%** | **15.21%** |
| **AMI Net** | **10.66%** | **19.13%** | **24.23%** | **15.32%** | **11.80%** | **13.82%** |
| Russell 2500 Growth | 7.17% | 15.78% | 23.13% | 17.96% | 12.88% | 14.63% |

*Not annualized. As of 9/30/18. Net returns are based on the highest annual fee paid by AMI clients of 1.25%. The annual fee schedule for institutional accounts is as follows: 0.90% for the first $10 million, 0.80% on the next $15 million, 0.70% on the next $25 million and 0.60% on the balance. The above information is based on the Domestic SMID Cap Growth Composite and clients accounts may vary and includes the reinvestment of dividends and other earnings. Past performance is not an indication of future returns. Please refer to important disclosures on last page. Source – AMI.

As seen in the table below, the top contributors to Q3 performance were Ligand Pharmaceuticals, Dave & Buster's, West Pharmaceutical Services, Anika Therapeutics and The Simply Good Foods Company. The bottom contributors to Q3 performance were Corcept Therapeutics, MGP Ingredients, Performance Food Group, LogMeIn Inc. and Innerworkings Inc.

**Top Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| Ligand Pharmaceuticals | 4.03% | 32.50% | 1.22% |
| Dave & Buster's | 3.04% | 39.44% | 1.11% |
| West Pharma Services | 3.85% | 24.53% | 0.88% |
| Anika Therapeutics | 3.12% | 31.81% | 0.86% |
| Simply Good Foods | 2.80% | 34.70% | 0.86% |

**Bottom Contributors in Q3**

| Company | Avg. Weight | Return | Contribution |
|---|---|---|---|
| Corcept Therapeutics | 1.88% | -10.84% | -0.25% |
| MGP Ingredients | 2.38% | -10.97% | -0.31% |
| Performance Food Group | 3.28% | -9.26% | -0.33% |
| LogMeIn Inc. | 2.65% | -13.39% | -0.37% |
| Innerworkings | 0.87% | -17.26% | -0.50% |

## Top Contributors

**Ligand (LGND)** -Ligand Pharmaceuticals reported another strong quarter driven by patient growth and indication expansion in the two main royalty generating drugs (Kyprolis from Amgen and Promacta from Novartis). The stock also rose on continued progression of the pipeline, including several large potential opportunities over the next several years.

**Dave & Buster's (PLAY)** -Following a challenging start to the year, Dave & Buster's has returned to solid growth, driven by a proprietary virtual reality (VR) game and improved food and beverage offerings. The company continues to open new stores with strong returns on investment. We believe that Dave & Buster's strong margins and traffic growth driven by additional VR games will lead to continued success.

**West Pharmaceuticals (WST)** - West Pharmaceutical Services reported strong quarterly results as the supplier of drug vial and syringe components is experiencing stabilized order patterns following a period of customer inventory reductions. After a period of capacity constraints, West expanded manufacturing to meet demand and customers reduced their inventory levels to coincide with shorter lead times. These reductions weighed on revenue during 2017 and into 2018 but have since improved. The growth outlook appears solid as West's products are integral components to many new drugs coming to market, especially in the faster growing biologics market.

**Anika Therapeutics (ANIK)** - Late in Q2, Anika's stock fell substantially after it announced that its next generation osteoarthritis treatment, Cingal, failed to provide a benefit over steroids. However, the stock recovered in Q3 after a better-than-expected earnings report and management commentary that it was committed to bringing this product to market. We expect to see final results of the trial late in 2018, which may ultimately show a benefit and thus we remain bullish on the name.

**Simply Good Foods (SMPL)** -Simply Good Foods reported strong results in the company's fiscal third quarter, with impressive double-digit revenue growth in what has been a generally challenging environment for packaged food. The company continues to benefit from a broader consumer shift to better-for-you, low carb snacking, with additional momentum driven by a new national marketing campaign. With plenty of distribution opportunities and the prospect of accretive M&A, we continue to like the stock.

**<u>Bottom Contributors</u>**

**Corcept Therapeutics (CORT) -** Corcept Therapeutics reported very good Q2 results but slightly lowered full year guidance. Corcept's main drug, Korlym, treats a rare disease called Cushing's Syndrome and a change in just a few patients per doctor can alter the revenue growth trajectory. We are not concerned with a slight change in guidance and we are bullish as Corcept will be advancing several new drugs in the pipeline that have substantial revenue potential in the next few years.

**MGP Ingredients (MGPI)** -MGP Ingredients reported second quarter earnings that were below expectations, driven by timing issues in shipments of aged whiskey to customers. In addition, the potential impact of retaliatory tariffs on bourbon (especially in the EU, a large export market) hurt sentiment on bourbon companies. However, the majority of MGP's customers are based in the United States, with the likelihood of any impact from tariffs negligible. MGP's markets continue to grow nicely, with many startups launching new brands every year. MGP should be able to grow earnings in the high-teens over the next few years as it supports customers with its inventory of aged whiskey, while also building its own brands.

**Performance Food Group (PFGC)** -Performance Food Group reported mixed fiscal Q3 earnings, with solid revenue and volume growth offset by higher operating costs. These higher costs were driven by a shortage of drivers, as well ongoing investments to build out the company's salesforce. Performance Food has gone through these types of investment cycles in the past, and the long-term revenue growth benefits outweigh the temporary contraction in profitability. We believe the company is well positioned to continue to grow volume with independent restaurants over the long term and we also like the diverse customer set (movie theaters, e-commerce, dollar stores) of Performance Food's Vistar subsidiary.

**LogMeIn (LOGM) -** LogMeIn Q2 revenue and EPS beat estimates but the company guided full-year results lower due to weakness in its core Collaboration business. When the company acquired the GoToMeeting assets, it began to implement new business practices with respect to pricing and renewals. While the intent was to drive overall revenue higher, the changes created some friction in the renewal process and LogMeIn's competition took advantage by offering various incentives to switch. Management believes it has identified the issues within its customer base and has implemented remedies. We believe that the shares are undervalued given the strength in its other businesses as well as the potential for improvement in Collaboration.

**InnerWorkings (INWK)** - In July, Innerworkings reported Q1 results that missed estimates driven by significant reductions in marketing spend at one of the company's largest clients. As a result, margins were pressured and management announced a cost reduction and business improvement plan. We saw significantly elevated execution risk following the announcement and decided to exit our position.

**<u>Portfolio Additions and Deletions</u>**

There were no portfolio additions in Q3; as noted above we sold Innerworkings.

Sincerely,

Your AMI Investment Management Team

*If at any time your current financial situation, investment needs or objectives change, please notify your portfolio manager promptly. Enclosed is a copy of the Proxy Voting Policies and Procedures. You may call or write us to obtain the latest copy of our ADV Part 2 and Privacy Notice. All attribution data is courtesy of Bloomberg.*