AMI Small Cap Growth Equity Quarterly Update

Growth Through Stability

Q3 ▪ 2024

Strategy Overview

The AMI Small Cap Growth strategy returned 6.55% (6.30% on a net basis) in Q3 versus 8.41% for the Russell 2000 Growth index. Asset allocation was the driver of the relative performance, with stock selection a slight benefit. Being overweight Consumer Staples and underweight Financials hurt performance, while being overweight Health Care was a slight offset. Outperforming stock picks in Health Care and Consumer Discretionary were partially offset by underperforming picks in Information Technology and Consumer Staples.

As seen in the table below, the top contributors to Q3 performance were Veracyte, Verona Pharma, Smartsheet, EXL Services, and Bright Horizons. The bottom contributors to Q3 performance were Braze Inc., PDF Solutions, PagerDuty, Madrigal Pharma, and e.l.f. Beauty

Top Contributors in Q3		
Company	**Avg. Weight**	**Contribution**
Veracyte	4.22%	2.14%
Verona Pharma	3.32%	2.07%
Smartsheet	4.03%	0.98%
EXL Services	4.21%	0.85%
Bright Horizons	2.94%	0.72%

**Please see last page for important disclosures.

Bottom Contributors in Q3		
Company	**Avg. Weight**	**Contribution**
Braze Inc.	2.17%	-0.37%
PDF Solutions	2.76%	-0.41%
PagerDuty	2.48%	-0.59%
Madrigal Pharma	2.74%	-0.75%
e.l.f. Beauty	1.20%	-0.76%

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Top Contributors

Veracyte reported a solid beat-and-raise quarter as the cancer diagnostics company has become the preferred solution in thyroid and prostate cancer outcome prediction. In addition, management reported more detailed adjusted income that allowed the Street to harmonize estimates, and the stock rerated higher. We believe this alleviates the issue of reporting good results and not getting credit due to mismatched analyst estimates.

Verona Pharmaceuticals stock rose dramatically on anticipation of being the first new treatment in many years for chronic obstructive pulmonary disease (COPD) where millions of patients are still suffering despite being on therapies. Verona's inhaled drug is additive to current treatments, which we believe is a key feature as it doesn't have to displace a competitor to be successful. For example, Management estimates that every 1% market share gain translates into $1 billion in revenue, a sizable opportunity for a company of this size that is now being reflected in the stock.

Smartsheet had a strong Q2, with subscription revenue and total ARR growing by 21% and 19%, respectively, both surpassing estimates. The company raised its full-year guidance, successfully increasing revenue and expanding margins. The stock rose following reports of talks with private equity firms and an official deal announcement came in late September. Given the acquisition, we exited our position.

EXL Services reported another solid quarter, with strong growth in Insurance and in Healthcare processing. The Analytics business also accelerated, which is encouraging due to its higher margins. The full-year guidance was adjusted modestly upward and the company continues to add new customers and leverage AI partnerships to meet the growing demand for generative AI projects.

Bright Horizons reported strong Q2 results, as the corporate child-care provider continues to see improving enrollment and utilization trends. The company's Back-up Care segment, which provides a safety net in case a child's primary caregiver is unavailable, turned in another quarter of 20% growth. Margins are also steadily improving, with room to return to levels seen before the pandemic.

Bottom Contributors

Braze reported a strong Q2, achieving profitability a quarter ahead of estimates and raising its full-year guidance, particularly for EPS. The number of customers increased, with more clients spending at least $500K, and net additions in the top tier reached an all-time high. However, there was a slight decline in net retention rates as pandemic-era contracts renew at lower levels, partly due to higher interest rates leading customers to conserve cash. More recent contracts, however, show significantly higher retention rates. The company believes this trend is nearing a bottom, and once it stabilizes, growth rates should normalize at higher levels. Additionally, Braze is gaining market share against legacy marketing platforms, attracting new customers thanks to its clear technology advantage.

PDF Solutions had an inline Q2, as no significant changes were anticipated. Last quarter, management announced it had begun shipping its new product to customers, which is expected to generate revenue in the second half of FY24. They reiterated expectations for 20% growth in that period and expressed satisfaction with customer progress. Early usage of these systems is high, which bodes well for future revenue. Margins expanded, and the royalty-based Integrated Yield Ramp division also showed sequential improvement. We remain positive about the company, given the promising second-half outlook, as PDF's products are essential to the semiconductor manufacturing process.

PagerDuty reported essentially inline Q2 results, with better margins and earnings despite slightly slowing revenue growth. The enterprise segment (large business customers) is performing well, while the small and mid-sized customer base has shown some volatility, although stabilizing trends emerged late in the quarter. This led to slightly lower full-year guidance, with some professional services revenue pushed to the following quarter. The company's renewed focus on enterprise customers has shifted revenue timing, as these businesses typically make purchases later in the year. PagerDuty expressed confidence in its ability to improve ARR growth back above 10% and anticipates an increase in net dollar retention.

Madrigal stock lagged in Q3 as the supplier of the first drug to treat fatty liver disease is being somewhat overshadowed by potential competition from GLPs. The company's drug was approved in July and while the opportunity is quite large given the serious nature and large patient numbers, investors will be closely watching competitor data out later this year. GLPs have so far not been effective at reversing liver fibrosis, and we believe they will be used early on in the disease, leaving Madrigal's drug to more serious patients.

e.l.f. Beauty reported solid Q1 earnings that were ahead of estimates but raised guidance by a smaller amount than investors were hoping. In addition, the company's sales that are tracked by Nielsen slowed during the summer. The company's make-up and skincare offerings have seen tremendous growth over the past few years and were bound to settle in the mid-teens range, while the business continues to grow faster internationally and in stores like Ulta and Sephora. We continue to like the stock as the company's inexpensive, but on-trend offerings should be an excellent fit for the current value-seeking consumer.

Portfolio Additions & Deletions

In Q3, we added GitLab, Kiniksa Pharmaceuticals, Primoris and Varonis. We sold BJ's Wholesale, PowerSchool, and Smartsheet.

GitLab is a comprehensive platform that streamlines the software development process by facilitating source code management and collaboration tools into a single application. This allows development teams to plan, build, test, and deploy software more efficiently. GitLab is critical to modern software development as it enhances collaboration among developers, fosters automation, and accelerates release cycles, enabling organizations to respond quickly to market demands and improve product quality. Its robust features help teams manage the entire development lifecycle, making it an important tool for both small startups and large enterprises. We believe the company can sustain strong +20% revenue growth while also expanding margins as it leverages AI and automation.

Kiniksa Pharmaceuticals is a supplier of the only approved treatment for recurrent pericarditis, a debilitating heart inflammation condition. The company has been growing quickly through increased adoption by doctors, who previously did not have many great tools for treating this condition. The company has a somewhat rare combination for a company of this size, a product on the market, no debt, and near profitability. While still several years away, Kiniksa has another interesting drug in the pipeline to treat autoimmune disorders.

Primoris provides infrastructure build and maintenance services to the utility, energy, renewables and pipeline markets. The company supports customers with engineering, procurement, construction and maintenance services. Primoris focuses on multi-year master service agreements, providing some predictability, with an expanded presence in higher-margin, higher-growth markets such as solar facility installations, power delivery systems, and communications infrastructure. We view Primoris as a long-term play on the upgrading of infrastructure in the U.S.

Varonis Systems is a leader in data security and analytics, focusing on protecting sensitive information across various environments. Its innovative solutions for data privacy, threat detection, and compliance make it key for organizations navigating today's complex digital landscape. Given the increasing demand for robust data protection due to stringent regulations and sophisticated cyber threats, Varonis has seen substantial growth. The company's recent expansion into AI further enhances its offerings and growth potential. Additionally, the shift to a subscription platform is boosting growth through new add-on products and improving cash flow, positioning Varonis as a key player in the cybersecurity sector with durable growth prospects.

BJ's became too large for the Small Cap strategy, and we saw better opportunities elsewhere

PowerSchool was acquired by private equity firm Bain Capital. As such we exited the position.

As mentioned previously, Smartsheet was acquired by private equity firms and we sold the position.

Disclosures

*Performance Disclosures: AMI Asset Management (AMI) is an independent investment management firm registered with the Securities and Exchange Commission since 1994. Registration does not imply a certain level of skill or training. AMI provides discretionary asset management services to institutional and individual clients through separately managed accounts using seven equity and fixed income strategies. The Domestic Small Cap Growth Composite includes all fully discretionary, fee-paying and non-fee-paying, taxable and nontaxable accounts with at least $100,000 in small cap equities on the last day of each previous quarter. The composite was created on October 1, 2008. Returns are presented gross and net of management fees and include the reinvestment of all income. Gross returns are presented before management fees but after all trading expenses. Net returns are calculated by deducting 1/4th of the highest applicable annual fee of 1.00% from the gross composite returns on a quarterly basis. Prior to July 1, 2019, net returns were calculated by deducting 1/4th of the highest applicable fee of 1.50% from the gross composite returns on a quarterly basis. Clients should not assume that managed accounts will attain similar investment performance in the future. All accounts are individually managed; therefore, returns for separate accounts may be higher or lower than the average performance stated above. The benchmark we use is the Russell 2000® Growth Index which measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values and includes the reinvestment of dividends. Index performance is provided as a point of reference only and does not imply that a Strategy will achieve returns, volatility, or other results similar to the index. The total returns for the index do not reflect the deduction of any fees or expenses which would reduce returns. Indices are unmanaged, and one cannot invest directly in an index.

**Source: AMI and Bloomberg. The top five and bottom five contributors information is based on a representative account taken from the AMI Small Cap Growth composite. The representative account was selected because it closely reflects the AMI Small Cap Growth investment strategy. Due to factors such as portfolio size, specific investment guidelines and inception dates of individual accounts, there will be dispersion between the weight, returns, and contributions of this account and other accounts in the composite. The Contribution is calculated by multiplying the weight (i.e., percentage of the total account) invested in each holding times the rate of return for that holding during the measurement period. The holdings identified do not represent all of the securities purchased, sold or recommended for AMI's clients. Actual client holdings and characteristics may vary and holdings are subject to change. The reader should not assume that (1) an investment in the securities identified was or will be profitable or (2) that the AMI Small Cap Growth Strategy will hold these stocks in the future. References to specific securities are not intended as representative of past recommendations by AMI. The securities shown should not be considered recommendations or solicitations and may not have been, or in the future be, profitable. Nothing presented herein is or is intended to constitute investment advice, and no investment decision should be made based on any information provided herein. Past performance is not an indication of future returns. There is a risk of loss from an investment in securities, including the risk of loss of principal.

To obtain free of charge (1) a complete list of composite descriptions, (2) the calculation's methodology and a list showing every holding's contribution to the overall account's performance during the measurement period, and/or (3) a complete list of all buy and sell recommendations for this strategy within the last 12 months, please contact Katharine Kim at (424) 320-4003 or katharine@amiassetmanagement.com.