
DF Dent 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 had a strong 2Q17 and has outperformed the S&P 500 for the year. 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. Within the Technology holdings in the portfolio, there are some excellent software stocks that are not household names, but have excellent growth opportunities and help mundane industries become more efficient. The positive aspects of the portfolio were offset slightly by stock selection in the Consumer Discretionary and Financial sectors.

Many of this year's top performing stocks in your portfolio 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. 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%.

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.

You may notice that D.F. Dent has implemented a new email encryption program that will require you to log into an email portal to view sensitive emails you receive from D.F. Dent (e.g., attachments with your portfolio appraisals or performance). This proactive step is part of our ongoing cyber security efforts to protect your personal information. Upon first receipt of an encrypted email from D.F. Dent, you will be invited to click on a link to set up a user name and password. This same information will need to be entered into the system each time you would like to access and view encrypted information from D.F. Dent. We take your privacy very seriously and believe that this extra step in reviewing our emails, while burdensome, will be worthwhile in keeping your sensitive information safe. If you have any issues or questions about the new system, please do not hesitate to call the office. We would be glad to walk you through the login process.

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)