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DF Dent Small Cap Growth Strategy

January 2018 Commentary

Portfolio Thoughts

Strong fourth quarter 2017 equity returns put an exclamation point on a standout year for equities. The S&P 500 total return for the year was 21.83%, its best year since 2013. Equities outperformed other asset classes including fixed income, WTI oil and gold. The big gains in 2017 were driven by a synchronized upswing in global growth, a corporate profit recovery and benign monetary policy. The fundamental picture continues to look positive with corporate earnings growth expected to continue in 2018.

For the fourth quarter of 2017, D.F. Dent's Small Cap Growth strategy returned 3.47% (gross of fees) vs. the Russell 2000 Growth Index total return of 4.59%. For the full year 2017, the total return from D.F. Dent's Small Cap Growth strategy was 16.91% (gross of fees), which underperformed the Russell 2000 Growth Index return of 22.17%.

Performance for the fourth quarter was negatively impacted by stock selection in the Consumer Discretionary, Health Care and Industrials sectors. Performance was also hurt by being overweight the Technology sector. The relative weakness in the Consumer Discretionary and Industrials was broadbased. This compares to the weakness in Healthcare, which was due to two specific stocks, Mesa Labs and AAC holdings. - comments on both stocks are below. These negative contributors were offset by positive stock selection in the Technology sector and our overweight position in Industrials.

4Q17

Ticker		Contribution To Return
	5 Highest	**1.76**
BECN	Beacon Roofing Supply, Inc.	0.61
SITE	SiteOne Landscape Supply, Inc.	0.36
PRO	PROS Holdings, Inc.	0.29
CVGW	Calavo Growers, Inc.	0.25
CSGP	CoStar Group, Inc.	0.25
	5 Lowest	**-1.21**
MLAB	Mesa Laboratories, Inc.	-0.44
EVTC	EVERTEC, Inc.	-0.24
AAC	AAC Holdings, Inc.	-0.19
LTRPA	Liberty TripAdvisor Holdings Inc Class A	-0.17
LAD	Lithia Motors, Inc. Class A	-0.16

The top three contributors during 4Q were:

- **Beacon Roofing Supply, Inc (BECN)** is one of the largest roofing and building materials distributors in the US. Its shares performed strongly in Q4 because the company reported a strong fiscal Q4 (calendar Q3) and confirmed positive market trends with healthy growth and potential for inflation (inflation is generally good for distributors). Management also issued a healthy fiscal 2018 guidance that looked conservative. In addition, the company will close its acquisition of Allied Building Products early 2018. The deal will be immediately accretive to earnings and the company's guided synergy seems to be conservative. All these factors combined drove significant outperformance by BECN in the last quarter

- **SiteOne Landscape Supply, Inc. (SITE)** is the only national distributor of landscaping products. Its shares increased significantly due to a Q3 earnings release that embedded very healthy business momentum despite weakness on the surface due to hurricane impact. If hurricane impact on the business was excluded, SITE's Q3 would have very solid organic growth and strong margin improvement. Management indicated that such trends will likely continue in 2018. In addition, management stated that the company has a very full acquisition pipeline, which will likely add significant growth and earnings accretion in 2018. That was why investors felt excited about SITE shares and lifted their prices to higher levels.

- **PROS Holdings (PROS),** a Houston-based provider of pricing and revenue optimization software, reported solid Q3 results. PRO beat all guidance metrics despite the disruption of Hurricane Harvey hitting its hometown, which contributed to strong Q4 share price appreciation. We continue to see PRO's core offering- data-driven price and revenue optimization software- as well positioned for secular growth. We added to our positions early in the quarter on weakness.

The top three detractors during 4Q were:

- **Mesa Laboratories, Inc. (MLAB)** manufactures instruments and consumables for healthcare, pharma, food and beverage industries. Its share price decline in Q4 was driven by a weak Q3 earnings release. The company reported a year-over-year decline in both revenue and earnings and missed consensus expectations due to the loss of a large customer and some manufacturing issues. Disappointing results combined with relatively high valuation led to significant share price under-performance in the quarter. But the company's longer-term investment thesis has not changed and its core business segments continue to perform well. Some of the issues in Q3 have been addressed and some will become increasingly less important going forward. That's why we continue to hold our positions in MLAB.

- **EVERTEC, Inc.** (**EVTC)** provides payment processing, merchant acquisition and business solutions to customers in Puerto Rico and Latin America. Its shares underperformed in Q4 because several hurricanes caused significant disruption to the economy of Puerto Rico, EVTC's main market. Despite a better-than-feared Q3 earnings release, the longer term impact of these hurricanes are difficult to predict. There is no clarity on the timing and scale of the rebuilding efforts and there is potential for long-term population loss due to emigration to mainland US. However, EVTC enjoys a dominant position in a fairly attractive business, uncertainty caused by hurricanes will eventually pass, the company will benefit from the eventual rebuilding of Puerto Rico, and its valuation is fairly cheap. That is why we continue to hold our EVTC positions.

- **AAC Holdings, Inc.** (**AAC),** a leading operator of inpatient and outpatient substance abuse treatment facilities, underperformed the market in Q4 despite fairly strong third quarter results and no meaningful negative news. We believe the weakness was due to year-end tax-loss harvesting. We recently visited the company's headquarters and met with its management team. AAC operates in a market with very significant and rapidly increasing demand, and management demonstrated a clear plan to stabilize the company and rejuvenate profitable growth. As such, we continue to hold our position in AAC.

Market Thoughts

The strong US equity performance in 2017 was indicative of many favorable trends. We are still in a bull market but recognize that we have had nine years of strong equity market returns. U.S. economic growth is accelerating. Corporate profits are growing nicely, as evidenced by the strong quarterly earnings reports we have seen this year. Additionally, corporate tax reform was just passed and should further aid US corporate competitiveness. We do not believe the current level of interest rates poses a threat to U.S. equities. In fact, it is precisely because the economy is doing well that the Federal Reserve felt confident that it could begin to normalize rates.

However, it is quite possible that many of these favorable trends are likely to shift in 2018. We believe the rate of profit growth will slow in 2H18 as corporate earnings, excluding tax reform benefit, will face tough year-over-year comparisons. The U.S. economy should return to more sustainable levels of growth. Interest rates may be 75-100 basis points higher. With the unemployment rate at the lowest level in seventeen years and the economy performing above potential for the first time in ten years, we also expect inflation to start creeping higher. The S&P 500 has not had a 5% correction for over a year, the second longest period in history without a 5% correction. Corrections within a bull market are healthy and the longer the markets continue without one is a cause for concern.

The bottom line is that liquidity, the lifeblood of the financial markets, is the key to the equity markets' future. We have had nine years of abundant liquidity thanks to an accommodative Fed. Expect this to change in 2018 as the Fed will no longer be growing their balance sheet. Instead, they will be shrinking their balance sheet, which is uncharted territory for the markets. While the Fed is being very cautious as their balance sheet shrinks, we do not know all of the ramifications of the Fed's actions. Where 2017 showed little to no volatility, investors should expect more volatility in 2018. As stock pickers, D.F. Dent views volatility as opportunity. We will be vigilant about using that volatility to the advantage of our clients.

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We appreciate the confidence you have placed in D.F. Dent and Co. We will continue to work diligently on your behalf.

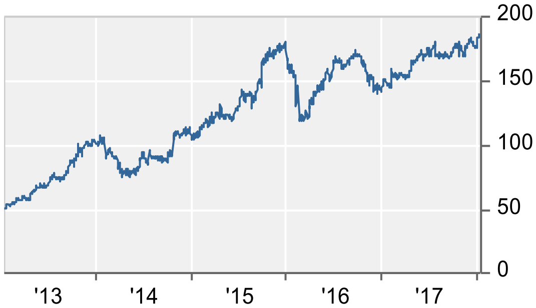
This commentary can be found on our website (www.dfdent.com). We encourage you to refer to our website for other information about our firm and our investment products, including our mutual funds.

Portfolio Profile:

Tyler Technologies, Inc. (TYL)

Tyler Technologies, Inc. - Closing Price

Source: FactSet



Share Price (1/16/2018):	$189.71
Shares Outstanding (mm):	39.3
Market Cap (mm):	$7,464
Operating Margin*	23.2%
Return on Assets*	9.5%
Return on Equity*	14.1%
Net Cash / Share	$4.83

* DFD 2017 projections, adding back amortization of acquired software and intangibles but not stock compensation expense.

Description:

Tyler Technologies, Inc., based in Plano, TX, and Yarmouth, ME, is the leading provider of software solutions and related services to state and local governments. TYL's software offerings address needs ranging from general ledgers to utility billing, parking tickets, school bus routing, jail management, jury selection, cemetery records, and property tax appraisals. TYL's sales range from a $30K project with a small town to a $36 million contract with the Cook County, Illinois (Chicago) courts. TYL couples best-in-class software with superior client support services.

Investment Rationale:

We view TYL as a well-managed and scalable company with one of the best businesses we know. We expect TYL to generate relatively consistent upper-teens earnings-per-share (EPS) growth over time as it grows revenues organically, expands margins through operating leverage, and deploys capital into acquisitions and stock buybacks. We expect the following attributes of TYL to generate sustainable stock outperformance going forward:

- Very Attractive Market: TYL sells mission-critical software to highly risk-averse organizations. TYL's strong customer service often leads to sales of additional modules and products.
- High Customer Retention Rates: TYL's annual revenue retention has exceeded 97% in recent years, excluding upsells. This is about as high as we have seen in the software space.
- Cross-Selling Opportunities Should Drive Customer Value-Added and Revenue Growth: Major cross-selling opportunities should emerge as TYL increasingly integrates its product offerings. For example, the integration of police, courts, and jail offerings should drive significant customer benefit.
- Increasing Percentage of Recurring Revenues: TYL's subscription and maintenance revenues, which are recurring in nature, represented 63.3% of revenues in the first three quarters of 2017. Some of TYL's other revenues, including software services and appraisal services revenues, tend to be somewhat consistent as well.
- Disciplined Capital Allocation Program / Strong History of Timely Buybacks: TYL has a stellar record of opportunistic M&A and repurchases. TYL has bought back 27 million shares since 2002.
- Clean and Strong Balance Sheet: TYL has $4.83/share in cash and no debt.
- Conservative Accounting: Unlike many software peers, TYL does not capitalize any R&D costs.