# Punch

## *Small Cap Commentary*
## *Second Quarter, 2020*

## *Overview*

The second quarter of 2020 saw a significant rebound from the declines of the first quarter, although this rebound has played out in some surprising ways. Given the unique nature of the pandemic and ensuing economic lock-down, few could have predicted the knock-on effects of this current crisis.

Some areas of the economy are obvious beneficiaries of virus fears and stay-at-home orders. For example, an e-commerce retailer selling unique handmade goods saw its sales double in the month of April, as consumers were couch surfing rather than mall walking. A home healthcare company should experience stronger demand as the elderly may be reluctant to move into assisted living or long-term care facilities. Healthcare and technology-related companies are benefiting the most from this pandemic.

Surprisingly, many consumer-related businesses are also seeing relatively strong demand today, in part because of government stimulus but also because Americans today have more free time and more discretionary spending after saving money on things like restaurants, travel, and entertainment (concerts, movies, etc.). The strength in boat sales, golf equipment orders, and the sharp rebound in new and used car sales has surprised us. New home construction also remains above expectations as housing supply is tight, and some urban dwellers are beginning to look for more space in the suburbs.

Of course, structural changes are inevitable on the other side of this recession, heralding in a new, more difficult reality for some companies. The need for commercial office space and the layout of workspaces will certainly shift as companies see the benefit of work-from-home arrangements. Small businesses (especially restaurants and retail stores) will likely struggle, as Americans increasingly adopt online shopping and delivery habits. Media consumption and advertising trends may also accelerate away from linear television and toward on-demand and social media.

While small cap stocks fell harder in the first quarter of 2020 than large caps, they rebounded faster in the second quarter. These companies, which tend to be more economically sensitive and more domestic than global, continue to reflect concerns

***Annualized Performance as of 6/30/2020*** *(net of fees)*

| | Q2 2020 | 1 Year | 3 Years | 5 Years | 10 Years | Since Inception* |
|---|---|---|---|---|---|---|
| Punch Small Cap | 29.57% | -10.79% | 0.54% | 2.53% | 9.53% | 8.70% |
| Russell 2000 Index | 25.42% | -6.63% | 2.01% | 4.29% | 10.5% | 7.33% |

*Inception date is 3/31/2002. Figures over one year are annualized.*

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*See disclosures at the end of this commentary* over the durability of the economic recovery. The Russell 2000 Index is off 13% on a year-to-date basis while the S&P 500 Index is down 3%. We believe that, after several years of lagging performance, small caps are an inexpensive investment in advance of an eventual economic recovery. Small cap value stocks are particularly attractive as their valuation is among the lowest in decades.

## Attribution

In the second quarter, the Punch Small Cap Strategy had a return of 29.7% compared to a benchmark return of 25.4%. The outperformance (+4.3%) came from a combination of both sector allocation (+2.9%) and stock selection (+1.4%).

Sector allocation was largely the result of a significant overweight to the consumer discretionary sector (13.1% average overweighting in the quarter) as consumer stocks returned 76% for the portfolio and 58% for the benchmark in the quarter. According to Furey research, this was the second highest absolute quarterly return for any small cap sector going back almost thirty-five years and reflects the surprising strength of consumer spending during the pandemic.

An overweight to financials (8.0% average overweight) hurt relative performance for the strategy, as this group rose 24.5% for the portfolio and 11.5% for the benchmark. Declining interest rates and rising credit concerns have weighed banks and other financial companies, and the sector continues to be down 26% on a year-to-date basis, with only energy stocks (-40% ytd) performing worse.

Notably, healthcare stocks continued their lead during the market rebound and this sector is now the lone small cap group to be positive for the year. Our significant underweight to this group (12.8% average underweight) has been a headwind to performance. Both the healthcare and technology sectors are the best-performing groups on a year-to-date basis (+6.4% and -0.5%, respectively) as they are obvious beneficiaries of this healthcare crisis and lock-down economy.

Despite the strong rebound in small caps in the quarter, growth stocks continued their outperformance over value stocks, rising 30.6% compared to 18.9% for value. On a year-to-date basis, growth stocks are down only 3.1% while value stocks are down 23.5%. This is one of the widest performance disparities on record between these two groups and leaves their relative valuations at extreme levels. A large part of the outperformance of growth in 2020 can be attributed to the fact that a majority (55%) of the Russell 2000 Growth Index is now made up of healthcare and technology stocks.

## Bottom Contributors to Return

**Varex Imaging Corporation (VREX, $592 million market cap)** was the biggest detractor from performance in the quarter by a large margin. Varex has been in the small cap portfolio since the third quarter of 2017, when we initially bought it shortly after it was spun-out of the large radiation oncology company Varian (VAR, $10.8 billion market cap). The company is a medical and industrial equipment business that designs, manufactures, and sells X-ray imaging components. We added to Varex in the first quarter, prior to its fiscal second quarter results. The expanded thesis behind our optimism was that the company would benefit from increased CT scans related to diagnosing COVID-19 cases. While CT scans helped the medical division grow in its second quarter, the rest of the business saw declines in revenue.

In our view, Varex has faced uncontrollable macro headwinds, like China trade tensions, but it also seems to run into execution issues more frequently than it should. A facility consolidation has been a lingering challenge for the company. We believe Varex has solid growth opportunities because of positive secular trends, but we need evidence of improved execution. We are watching to see Varex return to historical operating margin levels, a key component of our original thesis for owning shares.

Another detractor for the strategy was **Deluxe Corporation (DLX, $984 million market cap)**. Best

**Bottom Contributors: Second Quarter 2020**

| Holding | Average Weight | Total Return | CTR** (bps) |
|---|---|---|---|
| Varex Imaging Corp. | 2.53% | -33.29% | -103 |
| Deluxe Corp. | 2.05% | -7.82% | -21 |
| Spok Holdings, Inc. | 1.65% | -11.49% | -18 |
| Enstar Group Ltd. | 2.17% | -3.95% | -15 |
| Drive Shack, Inc. | 0.13% | -24.34% | -14 |

***CTR represents the contribution to total return in basis points. Contribution data is reflective of a representative account in the Punch Small Cap Equity Strategy.*

known as a check company, DLX has diversified meaningfully over the years into small business services. The company hired a new CEO, Barry McCarthy, a little over a year and a half ago. McCarthy has an impressive background and, we believe, the turnaround experience the company needs. With a new management team in place, the company began its shift by focusing on sales-driven growth versus prior management's emphasis on acquisition-oriented growth. Turnarounds are difficult, but they become particularly challenging when the macro environment runs into an unusual circumstance like a pandemic. Beginning in mid-March 2020, small businesses around the country began to see demand plummet as a result of the government mandated closures to mitigate the virus's impact. Deluxe has over 4.5 million small business customers, but it remains unclear which will survive the economic impact of COVID-19, and that uncertainty is reflected in DLX's share price today. In the first quarter, DLX had revenue declines in three of four segments and operating margin deleverage. We are eagerly waiting for Deluxe's next update on small business and the impact it may have on the company's long-term target of sales growth without acquisitions.

**Spok Holdings, Inc. (SPOK, $178 million market cap)** is a healthcare communications company that designs and sells software for hospital staff communication through several mobile modalities. SPOK's legacy pager business has been in secular decline for years but continues to provide solid cash flow to fund the development of its software platform. After being a top contributor to performance in the first quarter of 2020 (driven mostly by a third-party takeout offer for $12 per share that was turned down unanimously by the bord of directors), SPOK faded in the second quarter. COVID-19 has hampered the launch of Spok Go, its new unified communications platform for healthcare systems, as customers struggled to manage their businesses with the impact from the virus. Management has communicated that 2020 is no longer expected to be a strong adoption year for the new platform because of COVID-19. Meanwhile, the pager business continues to decline, and activist shareholders are becoming more vocal. We continue to hold shares to see what comes from the activist campaign.

## *Top Contributors to Return*

The top contributor to performance during the second quarter was our investment in the e-commerce platform **Etsy, Inc. (ETSY, $12.6 billion market cap)**. We first took a position in Etsy during 2016 and have watched this unique two-sided marketplace grow to become the dominant player in handmade home goods, jewelry, art, and other unique items. In 2017, Etsy hired a new CEO and CFO that we believe have done an excellent job driving growth and focusing the business on being a special platform connecting millions of sole proprietors and small businesses to a group of buyers that value their creations and stories.

During the quarter, Etsy released an extraordinarily strong outlook bolstered by the shift towards e-commerce, support for small businesses, and customers craving a human touch to their online shopping experience during the pandemic. Additionally, there was a tremendous surge in sales of a new product category for the website, handmade fabric facemasks. While we do not expect the current level of sales growth to be sustained indefinitely, the company should benefit long-term as the millions of new customers introduced to the platform in recent months become repeat buyers. Etsy remains profitable, well capitalized with a net cash balance sheet, and has numerous growth opportunities on which the proven management team may execute in the coming years.

The second largest contributor to performance was **StoneX Group Inc. (SNEX, $1.06 billion market cap)**. After completing its acquisition of GAIN Capital during the quarter, INTL FC Stone renamed the business "StoneX Group." INTL FC Stone is a financial services platform that provides services such as hedging, commodity trading, and global payments, among others.

*Top Contributors: Second Quarter 2020*

| Holding | Average Weight | Total Return | CTR** (bps) |
|---|---|---|---|
| Etsy, Inc. | 4.94% | 176.35% | 555 |
| StoneX Group, Inc. | 6.03% | 51.68% | 278 |
| Callaway Golf Co. | 4.38% | 71.44% | 275 |
| Malibu Boats, Inc. | 2.90% | 80.44% | 199 |
| Lithia Motors, Inc. | 2.72% | 85.54% | 199 |

***CTR represents the contribution to total return in basis points. Contribution data is reflective of a representative account in the Punch Small Cap Equity Strategy.*

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In February, INTL FC Stone announced they would acquire GAIN Capital to form a combination that will broaden both the product offerings and list of customers for both companies while expanding customer float by roughly $1 billion. After closing the deal in June, StoneX Group now has GAIN's digital platform and global footprint that boasts over 140,000 new clients in over 180 countries. Additionally, the combined businesses have several duplicate operations that the company can eliminate, which we expect to help enhance margins and the earnings profile of the business over time. On top of making a considerable acquisition, StoneX Group reported a record quarter benefitting from extreme volatility in the markets. We believe that the combined entity is now positioned to drive meaningful earnings improvement in the coming years, and the company remains "under the radar" with not a single sell-side analyst covering it.

After qualifying as one of our top detractors last quarter, shares of **Callaway Golf Company (ELY, $1.655 billion market cap)** rebounded and became a top contributor this quarter. This golf equipment and apparel manufacturer benefitted during the quarter from encouraging statistics and trends happening in the golf industry, despite the ongoing global pandemic. While COVID-19 has paused countless activities across the world, golf represents one of the few group hobbies that most areas still permit. During May, the number of scores posted to the U.S. Golf Associations network was up 22% from a year ago and total rounds played in many cities rose more than 20% in late May and early June. We believe this resurgence is partly driven by new participants picking up the sport that has been labeled as "dying" for decades. While Callaway is not immune to COVID-19's widespread disruption, we believe the company is in a favorable position to continue growing over the long term. Today, we believe that Callaway has an enviable market leading brand, strong balance sheet, and a management team with a demonstrated ability to drive organic growth.

## *Portfolio Activity*

The Punch Small Cap Strategy ended the quarter holding a total of 45 positions, with four new additions and four exits in the portfolio. While the first quarter of 2020 did not see significant trading activity in the strategy, the second quarter experienced increased repositioning.

Total turnover in the Punch Small Cap Strategy stands at 25.9% since inception, and its active share exceeds 98%. Our top ten holdings accounted for 40% of the portfolio at quarter's end, with StoneX Group Inc. qualifying as our largest position at 6.6%.

We added two healthcare companies to the portfolio in the quarter, **Phibro Animal Health Corp. (PAHC, $1.3 billion market cap)** and **BioSpecifics Technologies Corp. (BSTC, $475 million market cap)**, while exiting one, **U.S. Physical Therapy, Inc. (USPH, $1.0 billion market cap)**.

Phibro Animal Health is a provider of livestock animal nutrition and health products, an industry that historically has enjoyed relatively stable end markets, high competitive barriers to entry, and strong profitability. While the company today has a $1.3 billion market cap, insiders own half of the company's shares, and family of the CEO has voting control through super-voting stock. Normally we look on such control arrangements with skepticism, but after meeting the CEO and CFO earlier in the year, we came away impressed with their thoughtfulness, passion for the business, and genuine alignment with shareholder interests. Despite its size, the company receives little attention from sell-side analysts, and we were told by management that our meeting with them at their New Jersey headquarters in January was more time than any analyst had spent with them in years.

Market disruption from the Asian swine flu (ASF) which wiped out a majority of the swine herd in China last year has pressured Phibro stock, but we believe there are signs that this disruption is normalizing, and the company itself is in process of developing its own vaccine for the disease. In addition, Phibro is quietly entering the companion animal market with a select number of new products that could be more meaningful in the years to come.

BioSpecifics Technologies is a pharmaceutical company that, we believe, is unique among small-cap biopharma companies. The company is profitable, generating free cash flow, growing, and has significant cash and no debt. The company receives royalty revenues from its pharmaceutical partners for collagenase, an injectable material that can treat the build-up of collagen in parts of the body. Current demand projections for the material reflect around 20% growth annually, and several potential new uses, including one for cellulite, appear promising. A new CEO joined the company this spring with an attractive track record in the industry, including selling his previous company to a large-cap publicly-traded pharmaceutical business. With only one boutique sell-side analyst covering the company, we believe the opportunity at BioSpecifics is underappreciated.

In April, we exited long-time holding U.S. Physical Therapy, a nationwide chain of physical therapy clinics. The company was one of our longest holdings in the portfolio with an initial purchase in 2011. Considering the challenges that social distancing has placed on discretionary healthcare like physical therapy, we took the opportunity to exit the position at what we believed was a fair value for the shares.

In May, we took a position in business development company (BDC) **Oaktree Specialty Lending Corp. (OCSL, $600 million market cap)**, a provider of debt financing to private middle market companies. The BDC is managed by L.A.-based asset manager Oaktree Capital Group, a well-known investor in distressed debt with a strong track record since taking over management of OCSL.

The company operates in the niche of publicly traded BDCs and, we believe, came into this crisis as one of the best positioned in the group. Oaktree Specialty Lending had one of the lowest leverage ratios in the industry and minimal troubled loans pre-COVID-19. Its portfolio is made of primarily senior secured debt, and the average borrower is sizable, with over $150 million of annual EBITDA.

During the market tumult of this year, Oaktree has been opportunistically adding investments in both secondary and primary markets while many peers were simply focused on supporting their existing companies. With shares trading at a 20% discount to net asset value and a sustainable dividend yield of almost 9%, we believe the shares are more than compensating for any potential credit risks in the portfolio.

In June, we added business services company **BrightView Holdings, Inc. (BV, $1.1 billion market cap)** to the portfolio. BrightView, a former private equity portfolio company that came public in 2018, is a landscape management company providing grounds maintenance services to large customers in the office, multifamily, and institutional sectors. The company is by far the largest in the country and is pursuing a consolidation strategy of acquiring and integrating smaller competitors who lack the scale and efficiency of BrightView. Most revenue for the company is contracted annually, and large corporate customers are unlikely to discontinue services despite disruptions caused by the current pandemic. The company has reasonable leverage, strong free cash flow, and a healthy growth pipeline. We initiated a position when a secondary stock offering pressured shares to what we believe was an attractive valuation.

In April, we exited **Drive Shack Inc. (DS, $115 million market cap)**, a golf entertainment company that we had owned in the portfolio since 2016. Drive Shack was a unique holding for us given its early stage development of golf entertainment venues around the country, but we believed that the success of competitor Top Golf and the company's excess cash and assets provided a foundation for growth that was underappreciated by most investors. In the spring, when most lock-down orders were in place around the country, Drive Shack closed all of its locations. This disruption, combined with a change in management strategy and stretched capital resources, caused us to exit the position entirely.

In the second quarter, we exited two of our four energy companies in the portfolio, **RigNet, Inc. (RNET, $40 million market cap)** and **Riviera Resources, Inc. (RVRA, $110 million market cap)**. Given the severe disruptions to the oil and gas sector, and meaningful impairments to asset values, we reduced our exposure to the sector and exited these smaller positions whose success, we believe, depended on a normalization that may be significantly delayed.

## *Conclusion*

While the outlook for the economy and market is obviously dependent on the path of the coronavirus epidemic, we are hopeful that over the course of the next year life will begin to normalize gradually. The road will certainly be bumpy and unpredictable, but as normalization eventually occurs, small cap companies should benefit. We believe that relative valuations for small cap stocks are attractive today, especially for value-oriented stocks, and we remain enthusiastic for the long-term prospects of smaller public companies.

Punch & Associates Investment Management, Inc. (Punch & Associates) is a registered investment adviser; registration as an investment adviser does not imply a certain level of skill or training. Information presented herein is subject to change without notice and should not be considered as a solicitation to buy or sell any security. Information presented herein incorporates Punch & Associates' opinions as of the date of this publication and is subject to change without notice. Forward-looking statements are subject to numerous assumptions, risks, and uncertainties, and actual results may differ materially from those anticipated in forward-looking statements. As a practical matter, no entity is able to accurately and consistently predict future market activities. While we make efforts to ensure information contained herein is accurate, Punch & Associates cannot guarantee the accuracy of all such information presented. Material contained in this publication should not be construed as accounting, legal, or tax advice.

Composite performance is shown net of fees and brokerage commissions paid by the underlying client accounts. Certain client accounts have directed us to reinvest income and dividends, while others have directed us to not reinvest such earnings. As such, performance data shown includes or excludes the reinvestment of income and dividends as appropriate, depending on whether the account has directed us to reinvest income and dividends. Past performance is no guarantee of future results, and investing in securities may result in a loss of principal.

Please refer to the attached Composite Profile and Schedule of Performance for information regarding Punch & Associates' compliance with GIPS® standards.

The reference to the top five and bottom five performers within the Punch Small Cap Equity Strategy portfolio is shown to demonstrate the effect of these securities on the strategy's return during the period identified. Punch & Associates calculated this attribution data using a representative institutional client account which: 1) imposed no material restrictions related to investments made; and 2) was fully invested in the Punch Small Cap Equity Strategy during the entire time period shown. The holdings identified do not represent all of the securities purchased, sold, or recommended for advisory clients during the period of time shown. Past performance does not guarantee future results; therefore, it should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list. Please contact Punch & Associates at andy@punchinvest.com or (952) 224-4350 to obtain details regarding our calculation methodology or to obtain a list showing every holding's contribution to the overall strategy's performance during the period of time shown.

We compile company specific information referenced in this commentary from a variety of sources including SEC filings, quarterly and annual reports, conference calls, conversations with management teams, and Bloomberg LP.

Any benchmark indices shown are for illustrative and/or comparative purposes and have only been included to show the general trend in the markets in the periods indicated. Such indices have limitations when used for comparison or other purposes because they may have volatility, credit, or other material characteristics (such as number and types of securities or instruments represented) that are different from those of the Composite and/or any client account, and they do not reflect the Composite investment strategy or any other investment strategies generally employed by Punch & Associates. For example, the Composite, or a particular client investment portfolio will generally hold substantially fewer securities than are contained in a particular index. *Inception of the Punch Small Cap Equity Strategy was March 31, 2002. **CTR represents the contribution to total attribution.

Punch & Associates Investment Management Inc.
Punch Small Cap Composite
Composite Profile and Schedule of Performance as of 6/30/2018

Punch

| Year | Annual Performance History | | | 3-Year Standard Deviation | | Number of Portfolios | Year End Composite Assets (mil) | Year End Firm Assets (mil) | % of Total Firm Assets | Dispersion[2] |
|---|---|---|---|---|---|---|---|---|---|---|
| | Gross of Fees | Net of Fees | Benchmark[1] | Composite[2] | Benchmark[2] | | | | | |
| 2002 (since 3/31) | -15.21% | -15.85% | -23.53% | N/A | N/A | 12 | $5.1 | $103.9 | 4.9% | N/A |
| 2003 | 55.66% | 54.22% | 47.25% | N/A | N/A | 29 | $12.9 | $167.3 | 7.7% | 6.8% |
| 2004 | 21.92% | 20.67% | 18.33% | N/A | N/A | 52 | $21.0 | $206.2 | 10.2% | 4.8% |
| 2005 | 13.01% | 11.81% | 4.55% | N/A | N/A | 67 | $23.8 | $258.7 | 9.2% | 3.3% |
| 2006 | 22.84% | 21.74% | 18.37% | N/A | N/A | 98 | $38.8 | $335.0 | 11.6% | 3.3% |
| 2007 | 3.64% | 2.66% | -1.57% | N/A | N/A | 272 | $103.9 | $397.0 | 26.2% | 3.7% |
| 2008 | -33.53% | -34.18% | -33.79% | N/A | N/A | 243 | $65.5 | $261.5 | 25.0% | 2.1% |
| 2009 | 32.65% | 31.40% | 27.17% | N/A | N/A | 257 | $85.2 | $340.4 | 25.0% | 3.3% |
| 2010 | 18.88% | 17.78% | 26.85% | N/A | N/A | 283 | $108.4 | $395.6 | 27.4% | 1.0% |
| 2011 | 0.80% | -0.13% | -4.18% | 20.7% | 25.3% | 284 | $113.6 | $475.6 | 23.9% | 0.7% |
| 2012 | 20.04% | 19.01% | 16.35% | 17.4% | 20.5% | 292 | $152.4 | $613.6 | 24.8% | 0.8% |
| 2013 | 42.63% | 41.54% | 38.82% | 13.6% | 16.7% | 320 | $266.1 | $832.7 | 32.0% | 0.9% |
| 2014 | -0.21% | -0.90% | 4.89% | 12.8% | 13.3% | 328 | $265.0 | $905.7 | 29.3% | 0.7% |
| 2015 | 0.51% | -0.39%[3] | -4.41%[3] | 15.7% | 14.2% | 330 | $254.7 | $938.1 | 27.2% | 0.8% |
| 2016 | 20.96% | 19.94% | 21.31%[3] | 17.6% | 16.0% | 350 | $307.4 | $1,101.0 | 27.9% | 1.2% |
| 2017 | 12.96% | 11.94% | 14.65% | 16.5% | 13.9% | 377 | $340.3 | $1,241.6 | 27.4% | 0.4% |
| 2018 (through 6/30) | 11.58% | 11.12% | 7.66% | N/A | N/A | N/A | N/A | N/A | N/A | N/A |
| Cumulative | 540.55% | 452.25% | 302.88% | | | | | | | |

| Period | Annualized Performance History | | |
|---|---|---|---|
| | Gross of Fees | Net of Fees | Benchmark[1] |
| 1 Year | 22.93% | 21.88% | 17.57% |
| 3 Year | 11.76% | 10.79% | 10.96% |
| 5 Year | 13.70% | 12.76% | 12.46% |
| Since Inception | 12.11% | 11.09% | 8.95% |

Punch & Associates Investment Management, Inc. (Punch) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Punch has been independently verified for the periods from April 1, 2002 through June 30, 2018. 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. The Small Cap Composite has been examined for the periods from April 1, 2002 through June 30, 2018. The verification and performance examination reports are available upon request. N/A indicates statistics are not required to be presented for the time period pursuant to GIPS.

The Composite creation date is December 31, 2005. The creation date is the date in which Punch started reporting returns at the strategy level while they had previously been reported at the account level.

1 - The Russell 2000 Index is the Composite's benchmark.

2 - See Note 7 for discussion of the composite dispersion and 3-year standard deviation calculation.

3 - According to Punch's Error Correction Policy, this Schedule of Performance has been updated from prior versions which incorrectly displayed the 2015 Composite TWR (net), 2015 Russell 2000 Index, and 2016 Russell 2000 Index figures as -0.26%, -5.11%, and 20.35% respectively.

## Notes to Composite Profile and Schedule of Performance

**Note 1. Organization and Nature of Business**

Punch & Associates Investment Management, Inc. (Punch) is an investment adviser registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940. The term "Firm," as defined by Global Investment Performance Standards (GIPS), represents Punch & Associates Investment Management, Inc.

The Punch Small Cap Strategy (Small Cap Composite) invests in U.S. listed public companies with market capitalizations between $250 million and $2 billion. Companies from the small cap universe are selected on the basis of economically attractive business models, accelerating fundamentals, cash flow characteristics, valuation relative to cash flow, and general investor recognition.

This description of products and services of the Small Cap Composite (the Composite) is not an offering. Past performance is not an indication or a guarantee of future results. Investments are subject to risk and may lose value. A list of our composite descriptions and our policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

**Note 2. Performance Presentation Standards**

This report includes all of GIPS' mandatory disclosures as well as additional disclosures deemed prudent by Punch's management. Investment philosophies did not change materially during the reporting periods or from period-to-period.

**Note 3. Accounting Policies**

All assets and liabilities in the Composite are reported on a fair value basis using U.S. Generally Accepted Accounting Principles. Investment transactions are recorded on a trade date basis. Dividends are reported on pay date basis. Punch's policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

**Note 4. Valuation Methodologies**

The Composite values all of its investments at fair value in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification 820 ("Fair Value Measurements") and the GIPS Valuation Principles. The Composite invests in Level 1 securities (i.e. marketable securities for which prices are readily available).

**Note 5. Calculation of Rates of Return**

The portfolio returns for the period are based in U.S. dollars and have been calculated using a time-weighted, monthly, geometrically linked rate of return formula to compute quarterly percentage returns. Each portfolio's monthly rate of return is the monthly percentage change in the market value, including earned interest and dividends, after allowing for the effects of cash flows.

The monthly composite rate of return calculation is weighted by beginning values. This results in an asset's size-weighted rate of return. Security transactions and any related gains or losses are recorded on a trade-date basis.

**Note 6. The Composites**

Punch has established composites for all fee-generating portfolios for which it has full discretionary investment decision-making authority. Punch's client base within the composites was comprised of institutional and individual investors with a minimum asset balance of $100,000. No alterations have been made to the composites as a result of changes in investment professionals. In addition, Punch is the investment adviser to transitory portfolios that were not eligible for inclusion in any composite because the portfolios are either new for the month first funded, or the portfolios had restructuring which took place during the month.

The Small Cap Composite is one of several composites managed by Punch. Punch's list is available upon request.

Performance is based on total assets in the portfolio, including cash and substitute securities. Generally, a portfolio will enter a composite on the first day of the first full month following its inception. A portfolio is removed from a composite as of the last day of its last full month. Historical performance results include the results of clients who are no longer clients of Punch. Each composite is comprised of separately managed portfolios.

The Composite is subject to Punch's large cash flow policy which defines a cash withdrawal of more than 10 percent of the portfolio's market value as a large cash flow which requires the Composite to be valued at the date of the withdrawal. This policy has been in effect for the periods from April 1, 2002 through June 30, 2018.

**Note 7. Composite Dispersion**

Composite dispersion measures represent the consistency of a firm's composite performance results with respect to an individual account's portfolio returns within a composite. Account dispersion is measured by the standard deviation from the central tendency (mean return).

The dispersion of the annual returns of the Composite is measured by the asset-weighted standard deviation method. Standard deviation attempts to measure how much exposure to volatility was taken historically by the implementation of an investment strategy. Only portfolios that have been managed for the full year have been included in the annual dispersion calculation of the Composite. Effective for the year ended December 31, 2011, GIPS requires the presentation of the three-year annualized standard deviation. This statistic measures the volatility of returns for the Composite and benchmark over the preceding 36-month period.

**Note 8. Investment Management Fees**

The net performance results set forth in the Schedule of Performance reflect the deduction of actual investment management fees. The standard fee structure is based on 1 percent of assets per annum on all discretionary assets unless otherwise specified. Prior to December 31, 2005, the fee structure was variable based on strategy and account size, not to exceed 1.5 percent per annum.

Account minimums and fees are negotiable on a case-by-case basis due to potential growth, size and services rendered.

**Note 9. Comparison with Market Index**

Punch compares its Small Cap Composite returns to a certain market index management believes has similar investment characteristics. The returns of this index do not include any transaction costs, management fees or other fees. This index is the Russell 2000 Index.