Daruma

Where Every Stock Counts®

FOURTH QUARTER 2018

PERFORMANCE COMMENTARY

SMID-CAP COMPOSITE

4TH QTR PERFORMANCE

	Contribution (%)
Best	0.91
Worst	-4.44
Best Minus Worst	-3.53
Rest of Portfolio	-16.45
Total Daruma	-19.98
Russell 2500	-18.49
Return Difference	-1.49

Dear Clients and Friends,

It was a brutal quarter for the Russell 2500, down -18.49%, and we fared worse, with the SMid-Cap Composite lagging the Index by an additional 149 bps, at -19.98%. We booked most of our underperformance in October during the market's first sharp break (-12.5% vs. -10.15%) but recovered to beat the Index in November and December by 17 bps and 57 bps respectively.

59% of the portfolio exposure did better than the Index, and we had five positions that generated a positive contribution, nothing to sneeze at in a market down so sharply. Regrettably the positions that trailed the Index weighed more heavily on performance than those that beat the Benchmark. We owned ten positions that detracted 100 bps or more from performance. In a market dominated by fear, any fundamental disappointment or any whiff of risk (e.g., less than pristine balance sheet, negative cash flow) triggered a supersized response on the part of investors.

As always, we are happy to discuss our fourth quarter results with you.

All the best,

Mariko

Mariko O. Gordon, CFA
Founder & CEO

All data is as of 12/31/18 unless otherwise noted. For important disclosure information, please see General Disclosures at the end of this presentation.

4TH QUARTER 2018

WINNERS AND LOSERS

SMID-CAP COMPOSITE COMMENTARY

Top Contributors

Company	Quarter End Position Size	Contribution
Agnico Eagle Mines	4.4%	0.61%
Etsy	2.6%	0.19%
LHC Group	2.8%	0.11%
Total		**0.91%**

AGNICO EAGLE MINES
Gold miner
+61 bps

ETSY
E-commerce marketplace
+19 bps

LHC GROUP
Home health care provider
+11 bps

Our best three stocks (gold miner Agnico Eagle Mines Limited (AEM) (+61 bps), e-commerce marketplace Etsy, Inc. (ETSY) (+19 bps) and home health care provider LHC Group (LHCG) (+11 bps) generated +91 bps in total contribution.

Agnico was up +19% in the quarter, more than the +7.5% increase in the price of gold. We believe 2019 could be a break out year for Agnico stock — the start of commercial production from the Meliadine mine means an acceleration in top line, reserve growth, as well as a substantial increase in free cash flow.

Etsy was up +13% on the back of strong earnings results. We believe Etsy is in the early innings of a multi-year growth opportunity as the leading online marketplace bringing together crafters and buyers of unique, handmade products. The company is focused on four key initiatives to drive sales and expand margins: 1) building trust and reliability; 2) enhancing search and discovery (ETSY has 50 million SKUS on its platform); 3) world class marketing capabilities; and 4) providing sellers with tools and services to help them grow.

LHC Group's stock (up +7%) recovered as uncertainty over changes in the Medicare reimbursement policies for its home health care services in 2020 was clarified. Investors now have increased confidence that LHC will continue to deliver healthy organic growth, driven by successfully integrating AFAM, a competitor that had chronically underinvested in technology (critical for future success in an outcomes and customer satisfaction driven age), but had

4TH QUARTER 2018

WINNERS AND LOSERS

SMID-CAP COMPOSITE COMMENTARY

Top Detractors

Company	Quarter End Position Size	Contribution
Ring Energy	0.0%	-1.57%
Aerie Pharmaceuticals	2.7%	-1.45%
Align Technology	2.1%	-1.42%
Total		**-4.44%**

RING ENERGY
Oil and gas producer
-157 bps

AERIE PHARMACEUTICALS
Glaucoma pharmaceutical supplier
-145 bps

ALIGN TECHNOLOGY
Orthodontic manufacturer
-142 bps

great and complementary geographic coverage. In addition we believe LHC will continue to add new hospital JVs, will expand existing partnerships, and will continue to boost growth through M&A.

Our three biggest detractors (oil and gas producer Ring Energy (REI) (-157 bps), opthalmic drug maker Aerie Pharmaceuticals (AERI) (-145 bps) and clear orthodontic maker Align Technology (ALGN) (-142 bps)) hit the portfolio by a total of -444 bps.

Ring is a conventional oil and gas producer in the Central Basin Platform in Midland, TX. REI was the proverbial baby thrown out with the bathwater in the fourth quarter's energy wash out. The Russell 2500 Energy sector was down -40% while Ring was down -59%. REI had many of the characteristics of those stocks hit hardest in the market meltdown — a smaller market cap, a hat size stock price, a 2018 miss relative to expectations, currently free cash flow negative (like most E&P companies), making it the victim of both tax loss selling and a buyer's strike in the selloff. Ring also happens to be debt-free, stewarded by a conservative management with a prior track record of success, owns superb acreage and is expected to be free cash flow positive in 2019, even at lower oil prices thanks to nimble, timely and aggressive cost cuts. By their nature, smaller E&P companies have more volatile quarterly results, something that can be hard to stomach in tough markets.

Aerie Pharmaceutical was down -41% in the quarter, compared to -26% for the Pharmaceuticals segment of the Index. While there was

absolutely no company specific fundamental reason for the weakness, AERI is an early stage company building a franchise in opthalmic drugs. With one newly launched drug for glaucoma and another awaiting approval, and still burning cash in the process, it fell victim to the "short the launch" investment strategy. The company has met its operational and sales milestones, and both Rhopressa and Roclatan (awaiting approval) are compelling drugs for a large and underserved market. While these may not be sexy and high-priced oncology drugs, the ophthalmic community is very excited about the effectiveness of these drugs. We added to our position, believing that 2019 results will prove the skeptics wrong.

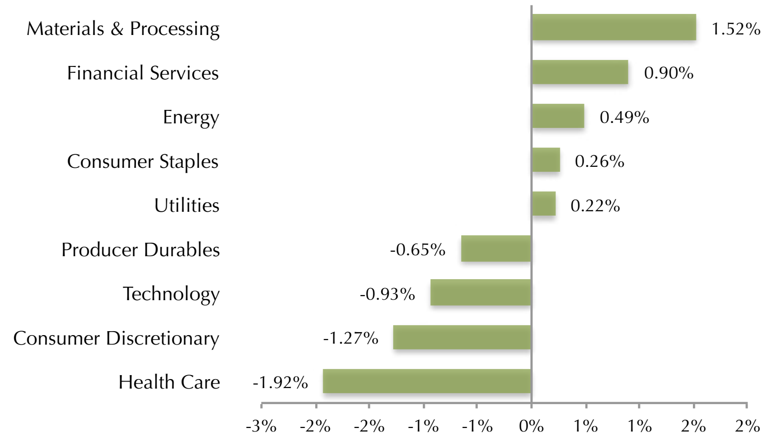
Align took a -46% hit in the quarter, due to a large and self-inflicted earnings whiff. Growth rates in case starts continue to be good, but an ill-conceived marketing promotion with a long tail, took a bit out of profits. We expect this hangover to continue through the first half of 2019. This atypical miss in what had been a stellar stock performer sporting a rich multiple, along with the spectre of more competition caused a collapse in a multiple that had been priced for perfection.

4TH QUARTER 2018

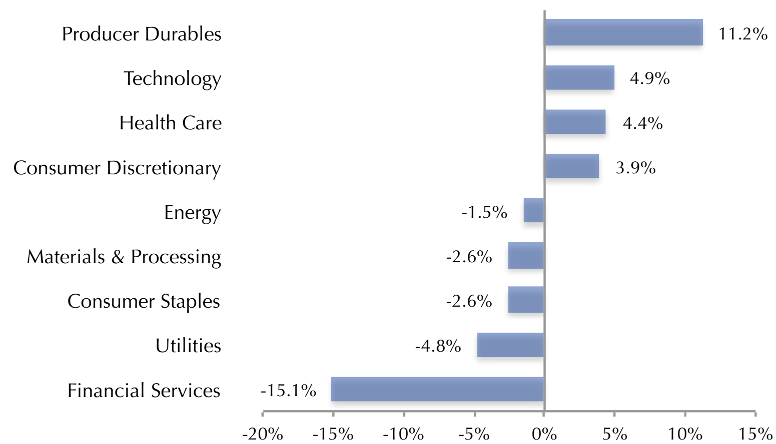
SECTORS OF NOTE

SMID-CAP COMPOSITE COMMENTARY

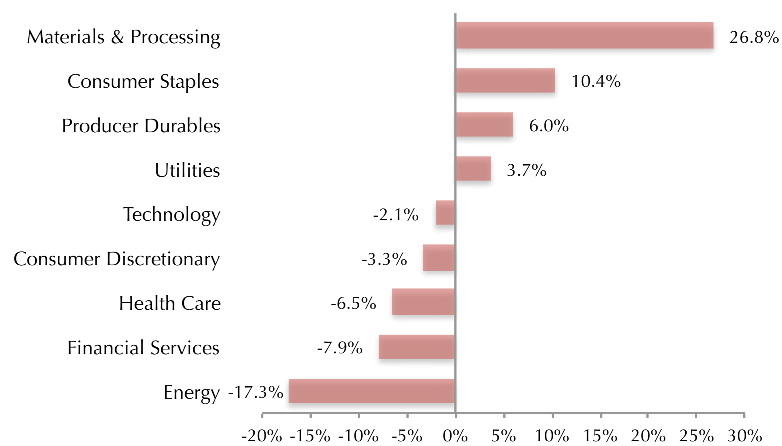
CONTRIBUTION DIFFERENCE DARUMA VS. R2500



DARUMA SECTOR OVER/ UNDERWEIGHT VS. R2500



RETURNS DIFFERENCE DARUMA VS. R2500



Sources: FactSet, Russell Investments & Daruma Capital Management

4TH QUARTER 2018

DECILE ANALYSIS

SMID-CAP COMPOSITE COMMENTARY

4TH QUARTER

It's safe to declare a market rout when the best performing characteristic is the lowest beta decile, down 7%, while the smallest decile is down a whopping 37%!

Anything that had a whiff of something undesirable — low liquidity, high short interest, high beta, low growth, and bad momentum, did far, far worse than the Index this quarter, down more than 30%.

A couple of anomalies stand out: the lowest P/Es fared poorly. Normally we'd expect inexpensive stocks to do well in a bad market. We believe deep cyclicals and banks were the culprits. Their low valuations did not protect them against investor fears that their economically sensitive earnings would be slashed in a recession.

The most popular stocks, as seen in analyst ratings and ownership concentration, suffered more than the out-of-favor wallflowers — a crowd heads to the exit, mayhem results.

4Q 2018

Decile	1	2	3	4	5	6	7	8	9	10
Market Cap (Largest to Smallest)	-12.1%	-14.2%	-18.2%	-18.6%	-18.7%	-21.2%	-22.0%	-20.6%	-23.6%	-37.1%
P/E Ratio (Lowest to Highest)*	-29.9%	-24.0%	-19.2%	-16.2%	-14.0%	-13.6%	-15.3%	-20.4%	-	-24.9%
Dividend Yield (Highest to Lowest)**	-19.0%	-14.0%	-15.7%	-14.9%	-16.6%	-	-	-	-	-24.4%
Short Interest (Lowest to Highest)	-14.3%	-15.4%	-18.7%	-18.0%	-20.4%	-18.8%	-22.9%	-22.0%	-25.7%	-30.0%
Beta (Lowest to Highest)	-7.0%	-10.9%	-15.2%	-17.8%	-19.4%	-21.8%	-23.8%	-27.6%	-30.5%	-32.3%
Sales Growth (Best to Worst)	-26.3%	-21.9%	-19.8%	-19.1%	-15.3%	-15.7%	-17.4%	-17.5%	-24.5%	-31.1%
Analyst Ratings (Best to Worst)	-22.7%	-24.3%	-23.1%	-22.4%	-20.9%	-20.3%	-19.9%	-17.7%	-19.2%	-20.7%
Institutional Ownership (Most to Least)***(*)	-22.0%	-22.8%	-20.1%	-21.2%	-20.0%	-20.0%	-21.6%	-20.7%	-19.3%	-18.4%
% Chg 1Q-3Q 2018 (Best to Worst)^	-26.0%	-18.9%	-20.2%	-17.5%	-16.5%	-16.1%	-19.3%	-20.8%	-23.7%	-28.9%
% Chg in 2017 (Best to Worst)^^	-25.2%	-21.6%	-18.7%	-18.0%	-17.4%	-16.8%	-16.7%	-18.0%	-20.6%	-31.6%

2018

Decile	1	2	3	4	5	6	7	8	9	10
Market Cap (Largest to Smallest)	7.1%	-5.6%	0.6%	-3.9%	-5.5%	-6.5%	-11.9%	-10.9%	-13.1%	-41.2%
P/E Ratio (Lowest to Highest)*	-31.0%	-22.4%	-14.6%	-6.6%	-3.7%	3.6%	10.8%	33.2%	-	-11.0%
Dividend Yield (Highest to Lowest)**	-18.6%	-11.6%	-11.4%	-6.1%	-4.5%	-	-	-	-	-7.1%
Short Interest (Lowest to Highest)	-8.9%	-6.7%	-9.3%	-9.1%	-11.3%	-7.8%	-7.8%	-5.0%	-3.6%	-20.1%
Beta (Lowest to Highest)	-3.6%	-5.4%	-7.2%	-10.9%	-13.1%	-16.2%	-13.8%	-18.0%	-12.0%	12.0%
Sales Growth (Best to Worst)	-0.7%	-1.9%	-5.7%	-7.6%	-5.3%	-6.4%	-10.7%	-12.0%	-18.6%	-32.1%
Analyst Ratings (Best to Worst)	-5.1%	-5.0%	-8.0%	-5.0%	-9.0%	-11.1%	-13.5%	-12.6%	-12.4%	-17.3%
Institutional Ownership (Most to Least)***(*)	-10.5%	-13.8%	-4.9%	-11.8%	-10.3%	-7.5%	0.5%	-6.9%	-9.3%	-15.4%
% Chg 4Q 2018 (Best to Worst)^	23.0%	7.1%	8.8%	-4.4%	-5.7%	-10.2%	-13.1%	-17.8%	-26.9%	-49.6%
% Chg in 2017 (Best to Worst)^^	-10.7%	-8.2%	-5.9%	-4.1%	-12.1%	-10.3%	-6.8%	-12.2%	-12.2%	-4.1%

Sources: Bloomberg, Russell Investments & Daruma Capital Management

The green indicates the best-performing decile for the category.

The red indicates the worst-performing decile for the category.

*Decile 10 of P/E Ratio category is made up of all stocks that have no P/E

**Decile 10 of Dividend Yield category is made up of all stocks that pay no dividend

***Institutional Ownership may be over/under stated due to timing of filings

****Institutional Ownership is as of the end of last quarter (if report completed intra-quarter)

^% Change in 1Q-3Q 2018 excludes stocks without complete performance

^^% Change in 2017 excludes stocks without complete performance

Note: Due to Russell Rebalance on 6/22/18 - actual benchmark returns may vary from decile results.

4TH QUARTER 2018

GENERAL DISCLOSURES

It should be noted that this presentation should not be construed as an offer or a solicitation of an offer to buy interests/shares in any investment fund managed by Daruma. Any such offer will be made only to qualified investors by means of a confidential Private Offering Memorandum and other operative documents, and only in those jurisdictions where permitted by law. Neither the Securities and Exchange Commission nor any U.S. State or international securities administrator has passed on or endorsed the merits of any such offerings of these securities, nor is it intended that they will. Any representation to the contrary is a criminal offense. The firm does not offer or provide tax or legal advice. Individuals are urged to consult with their own tax or legal advisers before entering into any advisory contract.

Past performance is not a guarantee of future results. Nothing contained in this presentation should be considered a recommendation to buy or sell any security. Due to rounding, certain performance numbers contained throughout this document may differ immaterially from actual performance, and may not add up precisely to the totals indicated for the same reason. Many factors affect performance, including changes in market conditions and interest rates, as well as other economic, political and financial developments. Performance for 2018 is not yet audited and subject to change upon audit. You should not assume that investment decisions we make in the future will be profitable or will equal the investment performance of the past.

A list of the Top Ten holdings by portfolio weight as of 12/31/18 is available on our website at http://www.darumanyc.com/portfolio/smid-cap. These holdings and certain other performance information contained in this presentation supplement the SMid-Cap Composite Presentation, which is available on our website at https://www.darumanyc.com/disclosures/equity-composite-presentation-smid-cap.

The portfolio is actively managed, so holdings, sector weightings and other portfolio characteristics may have changed since the dates shown. They should not be considered recommendations to buy or sell any security. You should not presume that any holding shown has been or will be profitable. The holdings referred to herein do not represent all of the securities purchased, sold or recommended for Daruma's clients.

The appropriate comparison benchmark for the SMid-Cap Equity strategy is the Russell 2500. The Russell 2500 includes approximately 2500 of the smallest U.S. common stocks based on a combination of their market cap and current membership in the Russell 3000. The Russell 2500 Value Index includes those Russell 2500 Index companies with lower price-to-book ratios and lower forecasted growth values, while the Russell 2500 Growth Index includes those with higher price-to-value ratios and higher forecasted growth values.

The SMid-Cap Equity strategy is a concentrated strategy that is not managed to a benchmark, so there are material differences in characteristics, such as the number of holdings and sector and industry weightings. In addition, benchmark performance does not include any fees or expenses. Because of these differences, benchmarks should not be considered a completely accurate comparison.

Several charts are included in the book to demonstrate certain information or conclusions. You should not make any investment decision relying only on these charts. Such charts are provided for illustrative purposes only and you should not make any investment decisions based on these charts or any other information contained within this presentation.

Performance information obtained from external sources may differ from those contained in this presentation. These differences may be attributed to various factors including, but not limited to: timing and pricing of transactions; weightings and holding periods of individual positions; different methods of analysis; different pricing sources; treatment of accrued income or different accounting procedures.

The information in this presentation is current as of the date of the presentation, unless otherwise noted, and may have changed by the time you read this. Daruma has obtained some of the information in this presentation from third-party sources we believe to be accurate. However, we do not assume any responsibility for or undertake independent verification of such information and we cannot guarantee the accuracy. Such third party information is footnoted.

Statements in this presentation that are not historical facts reflect our opinions, beliefs or expectations as of the date of this presentation. Subsequent events may impact whether those come to pass. This presentation is the property of Daruma. The contents of this presentation are confidential. By accepting or reading any portion of this presentation, you agree that you will treat the presentation confidentially.

This presentation is intended for review purposes only by the person(s) or organization(s) to whom it is given and Daruma expressly prohibits its redistribution, dissemination or sharing, in part or in its entirety, to other person(s) or organization(s) without Daruma's prior written consent.