Where Every Stock Counts®

FOURTH QUARTER 2018

PERFORMANCE COMMENTARY

SMALL-CAP COMPOSITE

Dear Client and Friends,

My sincere apologies for the delay in sending out this 4Q 2018 quarterly commentary — the perfect storm of issues thwarting timeliness are too long and tedious to delve into — the unintended benefit is that we can share that January's performance was strong, with the Daruma Small-Cap Composite up +14.54% vs. +11.25% for the Russell 2000, for a relative gain of 329 bps. January's performance reflects the Market's 180 degree reversal — what was loathed in the portfolio in December became a hot commodity in January.

4TH QTR PERFORMANCE

	Contribution (%)
Best	0.27%
Worst	-4.38%
Best Minus Worst	-4.11%
Rest of Portfolio	-20.75%
Total Daruma	-24.86%
Russell 2000	-20.20%
Return Difference	-4.66%

It was a brutal fourth quarter for the Russell 2000, down -20.2%, and we fared worse, our Small-Cap Composite coming in at -24.86%, trailing by 466 bps. Only 43% of our portfolio exposure did better than the Index, and we had only two positions that generated a positive contribution, something not altogether surprising in such a vicious market slide. We owned 12 positions that detracted 100 bps or more from performance. In a market dominated by fear, a wide range of characteristics made pariahs out of stocks (e.g., less than pristine balance sheet, negative cash flow, operating turnaround, tax loss selling, expensive winners) and triggered a supersized negative response on the part of investors. The sectors that did best in the quarter, Utilities (-7.2%), Consumer Staples (-15.1%), and Financial Services (-15.7% — REITs notably were down only -10.9%) are also the sectors in which we are most underweight, which explains in part why the broader portfolio lagged the Benchmark.

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

SMALL-CAP COMPOSITE COMMENTARY

Top Contributors

Company	Quarter End Position Size	Contribution
Tandem Diabetes	2.8%	0.26%
Planet Fitness	5.1%	0.01%
Total		**0.27%**

TANDEM DIABETES
Insulin pump maker
+26 bps

PLANET FITNESS
Budget fitness centers
+1 bps

Our two positive contributors — insulin pump maker Tandem Diabetes (TNDM) and budget fitness chain Planet Fitness (PLNT) — generated 27 bps of contribution. Our three biggest detractors — wireless spectrum provider Boingo Wireless (WIFI), golf equipment and apparel maker Callaway (ELY) and women's health pharmaceutical company TherapeuticsMD (TXMD) detracted 438 bps. The net detraction of our best and worst stocks was -411 bps, making up the bulk of our underperformance. The rest of the portfolio was down -20.75%, a skosh more than the Index at -20.2%.

We bought Tandem Diabetes under pressure in the market meltdown, and profited from a 15% rebound in the stock. Tandem is an example of a fast growing company whose stock had been a big winner and had gotten expensive. In order to fund its growth it is a net cash consumer, and stocks like these were hit hard in the market meltdown. We found the entry point to be compelling, and when investors decided that perhaps the end of the world was not coming, owning a company with growth drivers independent of global macro factors became more attractive, and we saw a nice price recovery. A more thorough discussion of Tandem follows.

Planet Fitness was essentially flat in the quarter (-0.75%) but generated +1 bps in contribution as we trimmed our position at higher prices. Despite being a high multiple stock, PLNT's high return, free cash flowing business model, and credible, long-term growth pathway helped buoy its stock price in the quarter.

4TH QUARTER 2018

WINNERS AND LOSERS

SMALL-CAP COMPOSITE COMMENTARY

Top Detractors

Company	Quarter End Position Size	Contribution
Boingo Wireless	3.1%	-1.50%
Callaway Golf	3.5%	-1.47%
TherapeuticsMD	3.5%	-1.41%
Total		**-4.38%**

BOINGO WIRELESS

Wireless network provider

-150 bps

CALLAWAY GOLF

Golf equipment and clothing

-147 bps

THERAPEUTICSMD

Women's health pharmaceutical company

-141 bps

Boingo Wireless was down 42% in the quarter after having jumped 54% in the previous quarter on a strong earnings report and the acquisition of Elauwit (which expanded its market significantly into student and large multi-family accounts). The 4Q decline was two-fold. First of all, investors reacted to 3Q earnings and guidance, which while good, raised some concerns around the growth rate of wireless carrier offloading. Second, the stock was swept up in the market meltdown of more expensive, free cash flow negative companies with unsure future growth rates. We believe that WIFI has successfully changed its business model to become a wholesale shared infrastructure/spectrum company that will be a huge beneficiary of 5G wireless, and feel that concerns around the rate of growth in carrier offloading will abate as contracts are renegotiated to reflect higher usage and higher caps.

Similar to WIFI, Callaway got hit hard after closing the prior quarter at a peak in stock price and valuation and after reporting terrific second quarter results. That reversed in 4Q and the stock was down 37%. While 3Q earnings were good, the stock took a pounding after announcing the acquisition of Jack Wolfskin, a European apparel maker. While ELY has made its long-term strategic vision clear (creating a portfolio of lifestyle brands beyond golf with acquisitions of TravisMathew and Ogio), the purchase of Jack Wolfskin was not viewed favorably by the Street. Despite impressive growth in sales, profits, cash flow and new product pipeline, the outgoing market tide further hurt Callaway. We believe that 2019's new product launches and good execution on the integration of Jack Wolfskin will drive the stock higher.

TherapeuticsMD was down 42% in the quarter. Although we remain extremely bullish on the company's long term prospects, the company is a poster child for what investors punished most in the fourth quarter market meltdown (early-stage, burning cash and controversial). TXMD remains our top pick for 2019. To recap our 3Q write up on the stock: in 2018, TXMD received FDA approval for three women's health products (Imvexxy for vulvar vaginal atrophy; Bijuva a bioequivalent hormone replacement therapy and Annovera a long-acting, procedure-free reversible birth control ring), of which only one (Imvexxy) has launched so far. The other two will be launched in 2019. All three products are compelling "better mousetraps" and priced competitively to existing products, including generics. Imvexxy's launch is going very well, with nine out of 10 of the largest commercial payors on board. Now, with claims adjudication revenues flowing in 1Q, we believe that TXMD will start to get some respect and see meaningful appreciation. We have done many cross checks and have spent a day with the entire management team (all seasoned pharmaceutical executives) who are beyond excited to be building out a women's health care platform at a time when large pharma has largely abandoned the space.

2018 PERFORMANCE

SMALL-CAP COMPOSITE COMMENTARY

The fourth quarter's results exacerbated what had already been a tough year, causing us to trail by 812 bps in total for the year, -19.13% vs. -11.01% for the Russell 2000. Our best three stocks (Planet Fitness (PLNT) +158 bps; rehabilitation, home health care and hospice provider Encompass Health (EHC) +76 bps; and pricing software SAAS provider PROS Holdings (PRO) +56 bps) contributed a total of +290 bps.

Our worst three holdings (oil services provider Select Energy (WTTR) -181 bps; oil and gas provider Ring Energy (REI) -178 bps; and Invacare (IVC) -158 bps) detracted -517 bps. The net detraction of our outliers was -227 bps. The rest of the portfolio detracted 585 bps more than the Index. We have since sold WTTR but are still optimistic about REI's long-term prospects.

We bought 15 positions and sold 14 in the year, not unusual for a year with such market turmoil. We are pleased with new idea flow and with the continual upgrading of the portfolio.

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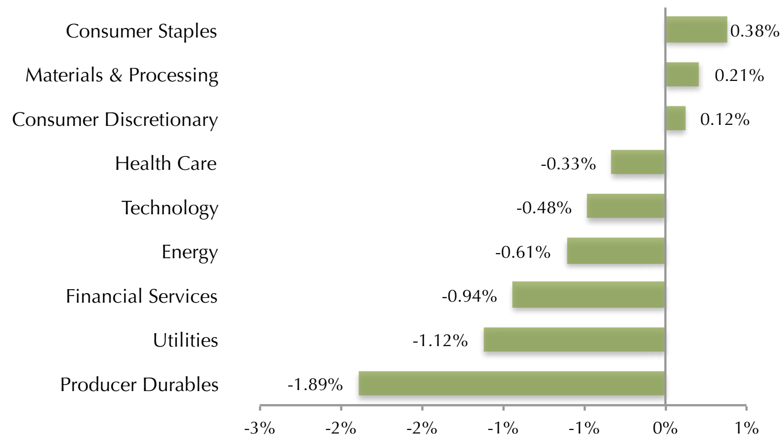
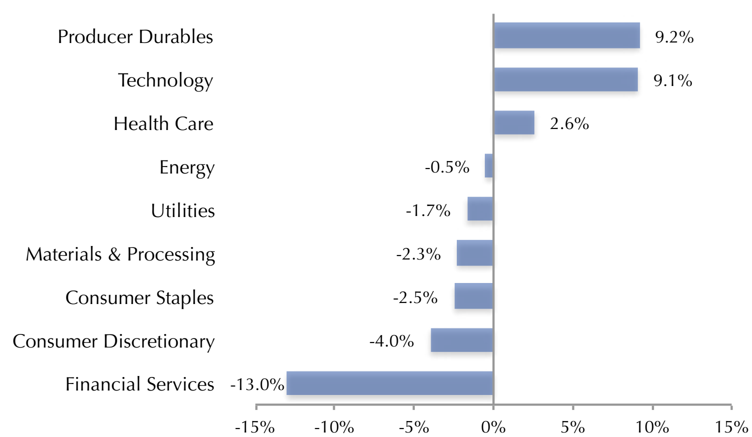
SECTORS OF NOTE

SMALL-CAP COMPOSITE COMMENTARY

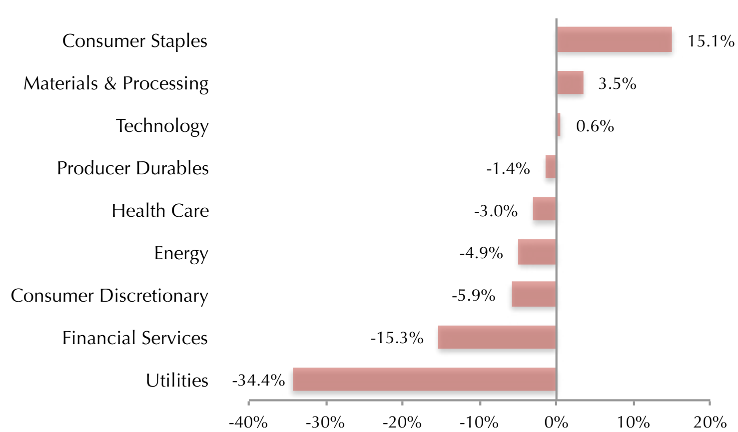
CONTRIBUTION DIFFERENCE DARUMA VS. R2000



DARUMA SECTOR OVER/ UNDERWEIGHT VS. R2000



RETURNS DIFFERENCE DARUMA VS. R2000



Sources: FactSet, Russell Investments & Daruma Capital Management

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DECILE ANALYSIS

SMALL-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)	-12.2%	-15.4%	-18.5%	-18.4%	-21.9%	-22.9%	-19.6%	-22.1%	-24.7%	-39.5%
P/E Ratio (Lowest to Highest)*	-31.0%	-23.9%	-19.0%	-15.9%	-14.3%	-14.5%	-18.1%	-	-	-25.4%
Dividend Yield (Highest to Lowest)**	-19.4%	-14.3%	-16.0%	-15.9%	-12.2%	-	-	-	-	-25.1%
Short Interest (Lowest to Highest)	-14.4%	-16.0%	-19.2%	-18.7%	-21.3%	-21.4%	-23.6%	-23.2%	-26.3%	-31.2%
Beta (Lowest to Highest)	-8.6%	-11.5%	-15.9%	-18.8%	-20.6%	-21.9%	-24.3%	-29.0%	-31.5%	-33.1%
Sales Growth (Best to Worst)	-26.8%	-21.7%	-20.3%	-20.1%	-16.2%	-16.3%	-18.1%	-18.6%	-28.6%	-33.0%
Analyst Ratings (Best to Worst)	-22.9%	-25.0%	-23.7%	-23.4%	-22.1%	-22.5%	-20.3%	-19.2%	-22.0%	-23.5%
Institutional Ownership (Most to Least)***(*)	-23.2%	-23.4%	-23.1%	-21.1%	-19.5%	-23.3%	-21.5%	-21.2%	-21.2%	-17.6%
% Chg 1Q-3Q 2018 (Best to Worst)^	-28.1%	-17.8%	-20.5%	-19.1%	-17.6%	-17.8%	-20.8%	-20.6%	-24.1%	-30.7%
% Chg in 2017 (Best to Worst)^^	-25.5%	-24.5%	-19.1%	-18.2%	-17.9%	-17.8%	-17.0%	-18.2%	-22.3%	-33.2%

2018

Decile	1	2	3	4	5	6	7	8	9	10
Market Cap (Largest to Smallest)	13.8%	7.0%	-4.9%	-5.0%	-5.4%	-13.9%	-6.4%	-17.0%	-13.3%	-45.7%
P/E Ratio (Lowest to Highest)*	-30.9%	-21.0%	-11.9%	-5.0%	-2.7%	6.6%	16.6%	-	-	-11.1%
Dividend Yield (Highest to Lowest)**	-18.6%	-11.5%	-10.1%	-4.7%	-0.5%	-	-	-	-	-7.4%
Short Interest (Lowest to Highest)	-10.5%	-5.8%	-10.3%	-8.5%	-10.2%	-8.0%	-8.2%	-2.6%	-5.6%	-20.2%
Beta (Lowest to Highest)	-5.5%	-6.0%	-7.5%	-10.9%	-13.9%	-15.6%	-14.2%	-17.0%	-10.5%	12.8%
Sales Growth (Best to Worst)	-0.3%	-0.8%	-6.3%	-8.3%	-5.0%	-6.1%	-9.8%	-13.1%	-21.7%	-29.7%
Analyst Ratings (Best to Worst)	-5.4%	-8.8%	-6.9%	0.1%	-9.1%	-11.0%	-13.7%	-13.9%	-15.7%	-22.5%
Institutional Ownership (Most to Least)***(*)	-11.2%	-12.8%	-9.1%	-7.3%	-8.3%	2.2%	-2.3%	-14.6%	-10.5%	-16.3%
% Chg 4Q 2018 (Best to Worst)^	24.0%	7.6%	9.1%	-2.0%	-7.5%	-10.1%	-7.7%	-22.8%	-27.7%	-51.5%
% Chg in 2017 (Best to Worst)^^	-11.6%	-8.4%	-6.6%	-3.6%	-12.9%	-8.4%	-8.9%	-12.4%	-12.3%	-1.5%

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.

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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/small-cap. These holdings and certain other performance information contained in this presentation supplement the Small-Cap Composite Presentation, which is available on our website at https://www.darumanyc.com/disclosures/equity-composite-presentation-small-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 Small-Cap Equity strategy is the Russell 2000. The Russell 2000 includes approximately 2000 of the smallest U.S. common stocks based on a combination of their market cap and current membership in the Russell 3000. The Russell 2000 Value Index includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values, while the Russell 2000 Growth Index includes those with higher price-to-value ratios and higher forecasted growth values.

The Small-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.

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