FAM FUNDS
Managed by
FENIMORE ASSET MANAGEMENT

# FAM Dividend Focus Fund

## Semi-Annual Shareholder Letter 2019

**June 30, 2019**

**Dear Fellow Dividend Focus Fund Shareholder,**

- The Fund changed its name from FAM Equity-Income Fund to FAM Dividend Focus Fund
- 31 out of 33 holdings in the Fund raised their dividends in the last 12 months[1]
- 12.9% is the average 5-year compound dividend growth rate for individual companies in the Fund as of 6/30/19[2]
- We are pleased with the Fund's performance as well as its industry ratings

The new name better reflects the Fund's steadfast focus since its 1996 launch. The FAM Dividend Focus Fund invests primarily in dividend-paying, mid-cap companies that have a history of consistently growing their dividend over time. Why dividends?

- Dividends can provide stability during turbulent markets and be meaningful to your overall investment returns.
- Businesses that pay dividends are typically healthy and generate more cash than they need for operations.
- A growing dividend starts with a growing company and can indicate the likelihood for future success.

The Fund continues to post solid performance numbers, both on an absolute and relative basis, rising 23.5% through June 30, 2019. The Fund has bested its benchmark, the Russell Midcap Index, by a solid margin year-to-date as well as over 1, 3, and 5 years. The Fund has also beaten the S&P 500 Index by a good margin over the same time periods. For the 10-year and since inception periods, the Fund trails its benchmark.[3]

So far this year, performance has been driven by three factors. Firstly, the market snapped back strongly after declining toward the end of last year and investor pessimism quickly turned to optimism. Secondly, our holdings in the Information Technology and Industrial areas performed very well. Both of the areas are heavily weighted in the portfolio and these holdings have appreciated over time while continuing to grow revenue, earnings, and cash flow. Lastly, there was a bidding war between two companies for one of the holdings in the Fund that drove the price up significantly.

Over longer periods, performance has come from selecting the right businesses, letting the compounders compound, and weeding out weaker holdings from the portfolio quickly. By not doing these things, it can be a detriment. For example, had we trimmed some of the larger positions last year, the Fund return this year would have been lower. Additionally, if we had held onto the underperforming companies that we sold last year, performance would have been lower. The Fund also benefitted from a number of other holdings being acquired at considerable premiums.

### Dividend Focus

Every Fund holding pays a dividend and the majority typically grow that dividend every year. In fact, on average, the companies in the Fund have increased their dividends 12.9% compounded over the last five years (as of 06/30/19).[4] We believe dividend growth is important because firms that are growing their cash flow are potentially able to grow their dividends. We favor investing in businesses that are growing their dividends quickly because it usually means the underlying operation is expanding and generating more cash than needed to reinvest back into the operation. These growing dividends contribute to the investment's total return.

[1] FactSet, as of 6/30/19
[2] FactSet, as of 6/30/19
[3] Bloomberg, as of 6/30/19
[4] FactSet, as of 6/30/19

**<u>Portfolio Activity</u>**

So far this year, the Fund has invested in 6 new names and added to 15 existing positions. Most of the new names we have known for years, if not decades. The sales were largely to upgrade the portfolio, reduce risk due to high valuation, or lock in a gain due to a merger agreement.

**Purchases**

The new stocks are: **Entegris (ENTG)**, **Genpact (G)**, **Fastenal Company (FAST)**, **The Hanover Insurance Group (THG)**, **First Hawaiian (FHB)**, and **Roper Technologies (ROP)**. We added to our positions in these holdings: **Broadridge Financial Solutions (BR)**, **Watsco (WSO)**, **Digital Realty Trust (DLR)**, **IDEX Corp. (IEX)**, **Marriott International (MAR)**, **Microchip Technology (MCHP)**, **US Ecology (ECOL)**, **Ingersoll Rand (IR)**, **EOG Resources (EOG)**, **Snap-on (SNA)**, **International Flavors & Fragrances (IFF)**, **Ross Stores (ROST)**, **Arthur J. Gallagher & Co. (AJG)**, **Stryker Corp. (SYK)**, and **Avery Dennison Corp. (AVY)**.

Here are the new holdings.

**Entegris (ENTG)** is a semiconductor materials business providing micro contamination filtration, specialty chemicals, and material handling products. Entegris' products enable semiconductor companies to advance to the next smallest node as well as improve production yields. We like this industry because the majority of their revenue is driven by growth in wafer starts rather than semiconductor prices. Entegris could likely make future acquisitions as well as grow their dividend.

**Genpact (G)** provides business process outsourcing (BPO) where they take over a customer's business operation (e.g., finance and accounting, customer service, IT) and run it at a lower cost without comprising quality. We like Genpact because of its potential long runway for growth in massively underpenetrated markets, deep customer relationships that provide long-term revenue streams, and the high returns it generates. This supports robust cash flow generation and shareholder-friendly capital allocation including more than $1.2 billion in stock buybacks over the last five years – plus a recently initiated dividend.

**Fastenal Company (FAST)** is a distributor we watched for years, but the stock was always too expensive for our taste. This year, despite Fastenal continuing to grow nicely, the valuation multiple contracted. We took advantage of the lower valuation to purchase an initial position in what we believe is a quality industrial distributor.

**The Hanover Insurance Group (THG)** is a property and casualty insurer which distributes through smaller independent agencies that value high service. The Hanover offers specialized insurance protection for small and mid-sized businesses, as well as homes and automobiles. We like this company because they have a strong partnership with select agencies and are able to help them grow. This, in turn, helps drive the firm's growth.

**First Hawaiian (FHB)** is Hawaii's oldest and largest bank, though the stock has only been publicly-traded since 2016 after it was spun out of BNP Paribas. First Hawaiian has more than $20 billion in assets and 60 branches, primarily in the state of Hawaii, along with the largest deposit share in the state at 36%.[5] The bank is efficiently run and has a conservative credit culture and low-cost deposit franchise. This is supported by a geographic location that helps insulate First Hawaiian from mainland competition.

We took a small position in **Roper Technologies (ROP)**. This holding has consistently grown faster than its industrial peers. We chalk this up to exceptional management that has positioned Roper in sustainable high-growth markets. We expect to add to this position over time.

**Sales**

**Versum Materials (VSM)** was sold after the stock appreciated significantly due to a bidding war to acquire it. Versum initially inked a deal to merge with Entegris. Shortly after the merger was announced, German company Merck KGaA submitted a substantially higher bid for Versum. The stock moved up near this higher bid, however Versum's management maintained that the Entegris merger was in the best long-term interests of shareholders. We decided to sell our shares and lock in our 75% year-to-date gain. Ultimately, the Versum board accepted an even higher offer from Merck. Once the dust settled, we bought shares in Entegris as a replacement for Versum (mentioned above).

[5] First Hawaiian 2018 Annual Report

**Penske Automotive Group (PAG)** was also removed from the portfolio. While this is a well-managed business, we believe the growth rate from here could be below its historical average due to the auto industry being near peak sales in our estimation.

**Stock Yards Bancorp (SYBT)** was liquidated as well. It was sold to buy the position in First Hawaiian, which we believe is a better performing bank with more attractive characteristics.

**Franklin Resources (BEN)** was sold as the firm has been a chronic underperformer. We do not see a near-term path for the company to return to its historical growth rates.

**Xilinx (XLNX)** was trimmed due to the stock appreciating too far ahead of our expectations. We estimate that the trim took some downside risk out of the portfolio, since this was a large position.

**Closing Thoughts**

We believe the Fund is well positioned to participate in future economic growth. We do our best to visit these companies each year and meet with management to understand their priorities and how they plan to grow their businesses. It is their track record of execution and bringing new products and services to the market that gives us confidence in the future. We are aware of current headwinds facing the economy and history demonstrates that a recession could come at some point, we just do not know when. However, we believe the best way to create long-term value is to let the compounders compound. This means not artificially contorting the portfolio because of a slowing economy, threats of new tariffs, or even political outcomes. We have spent a great deal of time studying the Fund's holdings and believe they have a long runway for growth. This should eventually translate into higher stock prices which means higher shareholder returns over time.

As always, we continue to work diligently on your behalf.

**Best & Worst Performers for 12/31/18 to 6/30/19***

| Top 5 Contributors | Average Weight (%) | Contribution (%) | Top 5 Detractors | Average Weight (%) | Detraction (%) |
|---|---|---|---|---|---|
| CDW Corp. | 6.54% | 1.85% | Robert Half Intl | 1.70% | 0.01% |
| Air Products & Chemicals | 5.34% | 1.66% | Entegris, Inc. | 2.88% | -0.02% |
| Ingersoll-Rand | 4.50% | 1.27% | First Hawaiian | 0.83% | -0.04% |
| Stryker Corp. | 4.94% | 1.20% | US Ecology | 1.74% | -0.08% |
| Xilinx, Inc. | 3.05% | 1.10% | National Instruments | 1.39% | -0.10% |

*This reflects the FAM Dividend Focus Fund's best and worst performers, in descending order, based on individual stock performance and portfolio weighting. Past performance does not indicate future results.*

**Performance (as of 6/30/19)**

| | YTD | 1-Year | 3-Year | 5-Year | 10-Year | Since Inception 4/1/1996 |
|---|---|---|---|---|---|---|
| FAM Dividend Focus Fund | 23.50% | 19.64% | 15.87% | 11.42% | 14.40% | 9.38% |
| Russell Midcap Index | 21.35% | 7.83% | 12.16% | 8.63% | 15.16% | 10.33% |
| S&P 500 Index | 18.54% | 10.42% | 14.19% | 10.71% | 14.70% | 8.78% |

*Past performance does not indicate future results.*

Paul Hogan, CFA
*Co-Manager*

Thomas O. Putnam
*Co-Manager*

*The opinions expressed herein are those of the portfolio managers as of the date of the report and are subject to change. There is no guarantee that any forecast made will come to pass. This material does not constitute investment advice and is not intended as an endorsement of any specific investment.*

*Performance data quoted above is historical. Past performance is no guarantee of future results. Current performance may be higher or lower than the performance data quoted. The principal value and investment return of an investment will fluctuate so that your shares, when redeemed, may be worth more or less than their original cost.*

**Reflects top contributors and top detractors to the fund's performance based on each holding's contribution to the overall fund's return for the period shown. The information provided does not reflect all positions purchased, sold or recommended for advisory clients during the period shown. It should not be assumed that future investments will be profitable or will equal the performance of the security examples discussed. Past performance is no guarantee, nor is it indicative, of future results. For more detailed information on the calculation and methodology as well as a complete list of every holding's contribution to the overall fund's performance during the time period shown, please call (800) 932-3271 or visit the fund's website at famfunds.com. Portfolio composition will change due to ongoing management of the fund. References to individual securities are for informational purposes only and should not be construed as an offer or a recommendation, by the fund, the portfolio managers, or the fund's distributor, to purchase or sell any security or other financial instrument. The summary is not advice, a recommendation or an offer to enter into any transaction with Fenimore or any of its affiliated funds. The portfolio holdings as of the most recent quarter*.

FAM DIVIDEND FOCUS FUND TOP 10 HOLDINGS

As of 6/30/19

| Name | % of Total Net Assets |
|---|---|
| CDW Corp. | 6.7% |
| Air Products & Chemicals | 5.5% |
| Stryker Corporation | 5.1 |
| Arthur J. Gallagher & Co. | 5.0% |
| Broadridge Financial Solutions | 4.9% |
| Microchip Technology, Inc. | 4.8% |
| Ross Stores | 4.7% |
| Ingersoll Rand | 4.6% |
| Avery Dennison Corp. | 4.2% |
| IDEX, Corp. | 3.5% |
| TOTAL NET ASSETS | $358,844,173 |

AVERAGE ANNUAL TOTAL RETURNS AS OF JUNE 30, 2019
The performance data quoted represents past performance.

| | SINCE INCEPTION | 10 YEAR | 5 YEAR | 3 YEAR | 1 YEAR | TOTAL FUND OPERATING EXPENSES* |
|---|---|---|---|---|---|---|
| FAM DIVIDEND FOCUS FUND | 9.38% (4/1/96) | 14.40% | 11.42% | 15.87% | 19.64% | 1.24%* |

** Disclosure: The Fund's total annual operating expense ratio as stated in the fee table of the Fund's most recent prospectus is 1.24%. The total operating expense as reported in the FAM Dividend Focus Fund's audited financial statements as of 12/31/18 is 1.23%. The Advisor has contractually agreed, until May 1, 2020, to waive fees and/or reimburse the Fund certain expenses (excluding interest, taxes, brokerage costs, Acquired Fund Fees and Expenses, dividend expense and extraordinary expenses) to the extent necessary to maintain Net Fund Operating Expenses for Investor Shares at 1.26%.*

*Past performance is not indicative of future results, current performance may be higher or lower than the performance date quoted. Investment returns may fluctuate; the value of your investment upon redemption may be more or less than the initial amount invested. All returns are net of expenses.*

*Please consider a fund's investment objectives, risks, charges and expenses carefully before investing. The FAM Funds prospectus or summary prospectus contains this and other important information about the FAM Dividend Focus Fund and should be read carefully before you invest or send money. The principal risks of investing in the fund are: stock market risk (stocks fluctuate in response to the activities of individual companies and to general stock market and economic conditions), stock selection risk (Fenimore utilizes a value approach to stock selection and there is risk that the stocks selected may not realize their intrinsic value, or their price may go down over time), and small-cap risk (prices of small-cap companies can fluctuate more than the stocks of larger companies and may not correspond to changes in the stock market in general).*

*To obtain a prospectus or summary prospectus and performance data that is current to the most recent month-end for each fund as well as other information on the FAM Dividend Focus Fund, please go to famfunds.com or call (800) 932-3271.*



*In part, the purpose of this presentation is to provide investors with an update on financial market conditions. The description of certain aspects of the market herein is a condensed summary only. This summary does not purport to be complete and no obligation to update or otherwise revise such information is being assumed. These materials are provided for informational purposes only and are not otherwise intended as an offer to sell, or the solicitation of an offer to purchase, any security or other financial instrument. This summary is not advice, a recommendation or an offer to enter into any transaction with Fenimore or any of their affiliated funds*

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