FAM FUNDS
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FENIMORE ASSET MANAGEMENT

FAM Small Cap Fund

Semi-Annual Shareholder Letter 2019

June 30, 2019

Dear Fellow Small Cap Fund Shareholder,

It is interesting to reread the letter we wrote you just six months ago. At that time, investors feared a variety of issues such as tariffs, labor inflation, the uncivil political discourse, and a Federal Reserve apparently still intending to raise interest rates while economic conditions were decelerating. As a result, small-cap stocks (Russell 2000 Index) declined -25.31% from their intra-day high on August 31 and ended 2018 down -11.01%. The FAM Small Cap Fund fell less, dropping -9.29% in 2018, and we were able to spend some excess cash buying shares at what we think should prove to be attractive prices.[1] It was a tense time for investors. The good news is that the Russell 2000 rebounded 16.98% in the first half of 2019 while our Fund returned 15.95%.[2]

In the last letter, we tried to outline that, while we did not know the timing, conditions would change and pessimism would likely subside if not outright swing to optimism.

> *"Meanwhile, there are reasons to be optimistic. Many of the problems facing us will likely be resolved. For instance, the U.S. and China may eventually strike a trade agreement with lower tariffs. Furthermore, the longer this uncertainty goes on, the more firms move sourcing to places such as Mexico, India, or Vietnam to avoid the China tariffs. Additionally, the Federal Reserve may decide that conditions no longer warrant further interest rate increases. It is quite possible that a year from now many of these issues may have passed. Humans certainly have their shortcomings, but they excel at adaptation."*

In our opinion, most of the factors that scared investors in late 2018 remain, but they seem to be more comfortable with the potential impact of items such as higher tariffs. Investors appear pleased that the Federal Reserve has now pivoted 180 degrees and many market observers expect them to lower short-term interest rates by year-end. If this happens, it could stimulate the economy.

Today, many investors could probably be described as "comfortable." They see several issues to worry about, yet the economy continues to chug along at a decent rate of growth as seen in statistics such as the GDP (Gross Domestic Product) and record low unemployment. Furthermore, we expect that they could be reassured by the Federal Reserve talking about potentially cutting rates to sustain economic growth.

Our point is that it is foolish, and virtually impossible, for us to try and predict short-term economic and political swings as well as investors' tastes. Our team does not speculate with your hard-earned capital – we seek and research great companies while following a time-tested investment approach.

We collect shares in what we deem to be quality businesses the way some people obsessively collect art or antiques. Our expectation is that our holdings should do well over the long term, even if they must navigate some difficult periods along the way. As always, we focus on what we believe are quality enterprises that are typically quite profitable and can grow even larger over time without losing the advantages that enable significant cash profits. Secondly, we want to invest only where management is both competent and honest in our opinion. Thirdly, we desire a strong financial position so that the company can survive, if not prosper, during any downturns that might arise. Finally, we are value investors and want to buy our shares at a discount to what we believe the business is worth.

[1] Bloomberg, 12/31/18: from the intra-day high on 8/31/18 to the 12/31/18 close
[2] Bloomberg, 6/30/19

Portfolio Activity

We found several interesting opportunities in recent months. Perhaps the hunting ground improved given the poor performance of small-cap stocks in general, particularly small-cap "value" stocks. While the small-cap universe is roughly 2,000 individual companies, most fail one or more of our criteria in terms of business quality, honest and capable management, a safe financial condition, and more. As a result, we focus our energies on a select group of what we estimate to be the highest quality companies – spending most of our time increasing our knowledge of these rather than trying to master the entire small-cap space. Our goal is to be prepared to move quickly when, for some reason, these firms are temporarily cheap. In that regard, we believe the first half of 2019 was productive.

Purchases

Often the easiest course of action is to take advantage of price declines and add to existing positions. These are operations we know well – in some cases having accumulated many years of study – so we are generally ready when the prices warrant additional purchases. During the first half of the year, we added to our positions in some of our favorite holdings such as **Carriage Services (CSV), CBIZ (CBZ), Colliers International (CIGI), Matador Resources (MTDR), Multi-Color Corp. (LABL), Natus Medical (BABY), Penske Automotive Group (PAG), and South State Corp. (SSB).** In each case, we believe our purchases were at a nice discount to our estimate of "economic value," which we define as either the present value of all future cash flows or the value of the enterprise to an acquirer.

Additionally, we invested in three new ideas that we are excited about.

Floor & Decor Holdings (FND) operates just over 100 flooring superstores and can grow much larger. While the average do-it-yourself customer or professional installer can go to Home Depot or Lowe's, a Floor & Decor store carries much more inventory and can provide substantial savings compared to the typical "mom-and-pop" flooring store. Their variety of options is astounding in our opinion. Simply put, Floor & Decor has a superior mousetrap. Thankfully, they are already quite profitable and leadership seems to be top-notch. The CEO started at Home Depot when he was 16 and rose to Chief Merchandising Officer before joining Floor & Decor. The combination of competitive advantages, growth potential, a clean balance sheet, and strong management is impressive from our viewpoint.

We realize that economic conditions may likely vary tremendously during the years ahead as they build toward their target of 400 stores, but think the potential justifies hanging on through the bumpy periods. Fears regarding tariffs played a part in recent share price volatility which gave us an opportunity to buy shares. While Floor & Decor does source some of their product from China, they access many global suppliers and are already rapidly shifting their supply chain (and raising retail prices) to offset the effect of tariffs. We might not know the full impact of tariffs for a while, yet believe any short-term issues should not change the fact that they are very profitable and can grow much larger.

Healthcare Services Group (HCSG) takes care of the mundane aspects of running various types of long-term care facilities – they literally clean the toilets, wash the clothes, and cook the meals. Thanks to the benefits of specialization, most of the time HCSG can provide these services at a lower cost than a facility can manage internally. There are approximately 23,000 long-term care facilities in the U.S. HCSG already runs the housekeeping services for 3,500 and dietary services for 1,500 – plus there are no meaningfully sized competitors. The business plan at HCSG is simple: approach long-term care facility operators and propose an outsourcing agreement that should save both the facility owner money and help earn a decent profit for them. This method has generated nice growth over the years (revenues grew from $603 million in 2008 to $2.009 billion in 2018) and we believe they can continue growing for many years.[3]

Our opportunity to buy shares arose because of troubles with some of HCSG's customers. Owning and running these facilities is a tough business at times. Operators build facilities planning on a certain percentage of beds being occupied and expecting reasonable reimbursement rates from federal programs such as Medicare. Conditions have been difficult. The majority of Baby Boomers are not quite old enough for these facilities. Instead, most residents are from the smaller in number pre-WWII birth years. Additionally, an increasing percentage of the elderly are staying in their homes longer, so when they get to assisted living they are there a shorter length of time and are sicker than the average resident of previous years. Finally, government reimbursement rates failed to keep up with inflation the past few years. As a result, several of HCSG's customers have struggled to pay their bills on time.

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[3] Healthcare Services Group 2018 Annual Report

The industry experienced similar challenges in the late 1990s, but conditions improved as operators made adjustments. Today, we see many signs of improvement including better demographic trends, a slowdown in new facility construction, and higher reimbursement rates. So, while the road is bumpy now, HCSG remains nicely profitable and we believe they should grow again soon.

Finally, late in the second quarter we purchased shares in **Entegris (ENTG)**. Entegris is a major supplier of chemicals and related filters and equipment to semiconductor manufacturers. Constructing a semiconductor involves multiple steps of depositing material in many layers. Each layer involves a variety of chemicals used to lay down material and then clean off excess materials between steps. Entegris has two macro trends going their way. First, the number of semiconductors produced is expanding as chips spread from traditional products, such as computers, to a wide variety of applications including appliances, automobiles, and data centers. Furthermore, as microchips grow in complexity, the amount of chemicals consumed increases. Additionally, the demand for better filtration improves in parallel. While semiconductor production will undoubtedly experience cycles, we believe the long-term trends of more and increasingly complex chips should allow Entegris to grow nicely.

Sales
We trimmed two positions – **Diamond Hill Investment Group (DHIL)** and **PC Connection (CNXN)** – while selling completely our positions in **Multi-Color Corp. (LABL)**, **ScanSource (SCSC)**, **US Ecology (ECOL)**, and **Winmark (WINA)**.

Our experiences in both **Multi-Color (LABL)** and **ScanSource (SCSC)** were disappointing. Whenever we purchase shares in a company we expect it to continue to be of excellent quality and – equally important – anticipate that management should continue making wise decisions. Both of these businesses did not live up to expectations. In the case of Multi-Color, they borrowed a lot of money to buy a very sizable competitor and then stumbled when combining the two entities. They then sold their entire operation to a private equity firm at what we think is a low price. For several years ScanSource, a distributor of electronic goods like barcode readers and credit card terminals, assured us profit margins would return to historical levels. ScanSource still has not registered a rebound in margins and we uncovered other signs that management is not up to our standards, so we sold our shares.

We finished selling our position in **US Ecology (ECOL)** early in the year. Our goal is to invest in 20 to 30 of the highest quality small companies we can find. Occasionally, we will sell a holding, not because anything is necessarily wrong, but because we believe we can invest in an even better enterprise. Such is the case here. While we expect that US Ecology should do quite well in the future, our team used the proceeds from the sale to fund some of our recent purchases like **Floor & Decor (FND)** and **Healthcare Services Group (HCSG)** which hopefully will perform even better.

Finally, we sold our few shares in **Winmark (WINA)**. Winmark owns brands they in turn franchise like Plato's Closet, Once Upon a Child, and Play It Again Sports. While we remain big fans of Winmark, we were never able to buy enough shares for the position to be material. As a result, the better alternative was to sell our shares and focus these resources elsewhere.

Closing Thoughts
It is an interesting time to invest in small businesses. "Growth" funds dramatically outperformed "value" funds during 2017 and 2018, and so far in 2019. We who study the markets company-by-company can see the impact in relative valuations. Dynamic, faster growing enterprises we characterized as too expensive a couple years ago trade at even higher valuations today. Additionally, many we would deem to be speculative, such as unprofitable biotechs, cryptocurrency providers, and cannabis firms, are attracting much attention. At the same time, many solidly profitable businesses with more modest growth rates have not seen the same type of jump in valuation multiples.

Many are wondering when will the trend revert? Will value ever outperform growth again? We are not foolish enough to say when, but experience, plus a knowledge of stock market history, assures us that these cycles reverse eventually. Furthermore, we are encouraged by many studies that have shown that value stocks historically outperformed growth stocks over the long term. To paraphrase a recent comment by a friend of ours, "How can buying something for less than it is worth ever be a bad idea?"

As always, we are grateful for the trust you place in us. Rest assured, we continue working hard 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 (%)
Frontdoor, Inc	6.69%	2.60%	CenterState Bank	4.25%	-0.11%
Hostess Brands	5.85%	1.42%	Diamond Hill	2.51%	-0.18%
Exlservice Holdings	4.97%	1.01%	Healthcare Services Group	1.93%	-0.18%
Colliers International	4.51%	0.99%	ScanSource	SOLD	-0.23%
Monro Inc.	4.71%	0.94%	Natus Medical	2.91%	-0.92%

This reflects the FAM Small Cap 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	Since Inception 3/1/2012
FAM Small Cap Fund Investor Shares	15.95%	-0.69%	8.27%	6.67%	11.04%
Russell 2000 Index	16.98%	-3.31%	12.30%	7.06%	10.85%
S&P 500 Index	18.54%	10.42%	14.19%	10.71%	13.28%

Past performance does not indicate future results.

Andrew F. Boord
Co-Manager

Thomas O. Putnam
Co-Manager

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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 SMALL CAP FUND TOP 10 HOLDINGS

As of 6/30/19

Name	% of Total Net Assets
Frontdoor, Inc.	6.7%
Hostess Brands, Inc.	5.8%
ExlService Holdings, Inc.	5.0%
Monro, Inc.	4.7%
Choice Hotels International, Inc.	4.7%
Colliers International Group	4.5%
CBIZ, Inc.	4.4%
Penske Auto Group, Inc.	4.3%
CenterState Bank Corp.	4.2%
Pinnacle Financial Partners	4.2%
TOTAL NET ASSETS	$181,283,672

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 SMALL CAP FUND *Investor Class* (3/1/12)	11.04%	N/A	6.67%	8.27%	-0.69%	1.29%*
Institutional Class (1/1/16)	11.11%	N/A	6.77%	8.42%	-0.58%	1.18%*

** Disclosure: The Fund's total annual operating expense ratio as stated in the fee table of the Fund's most recent prospectus is 1.29% after fee recoupment of 0.01% for the Investor Class. The Fund's total annual operating expense ratio as stated in the fee table of the Fund's most recent prospectus is 1.18% after fee recoupment of 0.01% for the Institutional Class. When excluding Acquired Funds Fees and Expenses, which are not direct costs paid by the Fund's shareholders and fee waivers, the total annual operating expense as reported in the FAM Small Cap Fund's audited financial statements for the Investor Class is 1.27% and the Institutional Class is 1.16% as of 12/31/18. 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 1.42% and Institutional Shares at 1.20%.*

Institutional Class shares became available for sale on January 1, 2016. For performance prior to that date, this table includes the actual performance of the Fund's Investor Class (and uses the Fund's Investor Class' actual expenses), without adjustment. The performance results shown on this and the next page for the periods prior to January 1, 2016, the date of commencement of operations for Institutional Shares, are for the Investor Shares, which are subject to higher fees due to differences in the shareholderadministrative services fees and certain other fees paid by each class. Institutional Shares and Investor Shares would have substantially similar performance results because the shares of each class are invested in the same portfolio securities of the Fund. Because of the difference in the level of fees paid by Investor Shares, the returns for the Investor Shares will be lower than the returns of the Institutional Shares.

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 Small Cap 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-capcompanies 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 Small Cap Fund, please go to famfunds.com or call (800) 932-3271.

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