

# Conestoga Small Cap Investors CCASX

Consistent.

## Morningstar's Take CCASX

**Morningstar Rating** ★★★★★

**Morningstar Analyst Rating** Silver

### Morningstar Pillars

Process	+	Positive
Performance	+	Positive
People	+	Positive
Parent	+	Positive
Price	+	Positive

### Role In Portfolio

Supporting

### Fund Performance CCASX

Year	Total Return (%)	+/- Category
YTD	18.86	2.06
2018	0.61	6.37
2017	28.44	6.94
2016	14.06	2.87
2015	8.03	10.44

Data through 9-30-19

10-08-19 | by Tony Thomas, Ph.D.

Capable execution amid strong inflows in 2017 and early 2018 kept Conestoga Small Cap's best features intact, earning a Morningstar Analyst Rating of Silver. The strategy is now closed to new investors.

Veteran manager Bob Mitchell is the linchpin of the team and its process. Mitchell cofounded Conestoga Capital Advisors in 2001 and has managed the fund since its 2002 inception. He navigated retirements from the firm's small investment team effectively by promoting comanager Joe Monahan in 2014 and hiring two dedicated analysts. Mitchell also comanages Conestoga SMid-Cap CCSGX, which extends this fund's process to slightly larger companies.

That process is sensible and clearly defined. The managers like firms with solid growth prospects and healthy balance sheets. They prefer businesses with the ability to grow earnings at least 15% per year

and generate 15% or more return on equity over the next three to five years. Low debt and decent insider ownership help. The team has proven faithful to these principles: The July 2019 portfolio easily topped both its typical small-growth Morningstar Category peer and its more-relevant Russell 2000 Growth benchmark on average return on equity, return on invested capital, and net margins--all while sporting a lower debt/capital ratio.

The portfolio's mix of profitable, growing companies has produced stellar results over time. Its trailing total returns through August 2019 were top-quartile over three, five, 10, and 15 years (and top 40% over one year), while its 12.4% annualized total return since inception bested the 9.9% peer average and the 10.9% index tally. Less-volatile returns also give the strategy a risk-adjusted advantage.

Capacity has been a worry but the team has responded well. Total assets more than doubled from early 2017 into mid-2018, and gradually closing to new investors (in March and July 2018) worked slowly. Yet throughout this stretch the managers maintained the portfolio's small-cap orientation and kept turnover in check. Such consistency is key to this strategy's attractiveness.

**Process Pillar** + Positive | Tony Thomas, Ph.D. 10/08/2019

A straightforward, well-executed approach earns a Positive Process rating.

Clear parameters guide the managers' search within the small-cap universe. They like firms with strong growth characteristics, including the ability to grow earnings and returns on equity at a 15% clip over the next three to five years. They also prefer firms with debt/capital ratios under 40%. Significant insider ownership (usually 10% or more) also gets their attention. Overall, the team's goal is to pick stocks

that have the potential to appreciate by at least 100% over the next three to five years.

The managers invest with conviction. They typically keep the number of holdings within a narrow range (45-55), and they tend to hang on to their picks for three to four years, on average. By mandate, the team must keep 80% of its assets in firms within the rolling three-year average market cap of the Russell 2000 Growth Index at the time of purchase, though they're willing to hold a company as it grows into mid-cap territory if they like its fundamentals. While the portfolio is generally well-diversified across individual holdings and sectors, the managers may deviate from the Russell 2000 Growth Index's sector weightings by up to 25 percentage points or twice the index's sector weighting (whichever is least). They also like to stay fully invested, often keeping cash levels below 5%.

The portfolio scores well on key quality metrics. Given the managers' preference for high returns on equity, the July 2019 portfolio's average ROE was 14.5%, surpassing the 9.8% small-growth Morningstar Category average and more-relevant Russell 2000 Growth Index's 5.1%. Their aversion to debt-ridden companies also stands out, with the portfolio's 30% debt/capital ratio well below the 38% mark for the typical peer and the index.

Sector weightings can veer widely from the index. The July portfolio's 34% technology stake was well ahead of the relevant index's 21%. On the other hand, it is often significantly underweight financials, which often don't meet the team's growth criteria.

The team is patient and willing to hold its best picks as they grow. The portfolio's average annual turnover rate in the five years through 2018 was a modest 17%, well below the typical peer's 83%. Indeed, long-term holdings make up a sizable portion of the portfolio: 46% of July's assets were in names held

for five years or longer. The team's largest holding by market cap in July was Tyler Technologies TYL at \$10 billion. Yet firms like Tyler are rare here, as the managers typically exit positions that reach \$6 billion in market cap. This preserves the portfolio's small-cap orientation. Many picks graduate into Conestoga SMid Cap CCSGX, with which this portfolio shared 30 holdings in July.

**Performance Pillar** + Positive | Tony Thomas, Ph.D. 10/08/2019

This fund looks good from various angles, earning a Positive Performance rating.

For starters, the fund has a solid record since its 2002 inception. From October 2002 through August 2019, its 12.4% annualized total return beat the 9.9% small-growth Morningstar Category average and 10.9% tally for the most relevant index, the Russell 2000 Growth. The portfolio's high-quality tilt yielded below-average volatility (as measured by standard deviation) and did not fall as far in down markets. This gave the fund a healthy risk-reward advantage: Its Sharpe and Sortino ratios, both gauges of risk-adjusted returns, easily topped the index and peer averages.

The fund's dominance shows over other time periods as well. Its trailing three-, five-, 10-, and 15-year total returns through August 2019 were top-quintile in the category. (Its one-year mark was in the top 40%.) Its rolling three-year returns since inception beat the relevant index in 63% of periods and its typical peer 77% of the time.

Even calendar-year 2014's ugly performance--its worst relative showing in the past decade--proved short-lived. The fund lost 8%--versus modest gains for the typical peer and the index--on poor stock selection in technology, healthcare, and energy. The managers pared weak energy holdings but stuck with their best tech and healthcare picks. The fund then swung to an 8% gain in 2015, beating 98% of its peers.

**People Pillar** + Positive | Tony Thomas, Ph.D. 10/08/2019

An experienced and thoughtfully constructed investment team earns a Positive People rating.

Comanager Robert Mitchell is key to the team's continuity. A 24-year industry veteran, Mitchell cofounded Conestoga with William Martindale in 2001. Together they comanaged this fund from its 2002 inception until Martindale retired in mid-2014. Joseph Monahan eased into Martindale's place alongside Mitchell during a yearlong transition. Monahan brings 37 years of industry experience to the team. The duo also taps Derek Johnston, Mitchell's comanager on Conestoga SMid Cap CCSGX since 2015, as part of the firm's general research process.

The managers have carefully fleshed out their research capabilities as the firm's assets have grown. Conestoga hired its first dedicated analyst, David Neiderer, in 2013, followed by Larry Carlin in 2015. These generalists support two low-turnover strategies (this one and smid-cap) whose modest portfolios and significant holdings overlap keep workloads manageable.

Manager ownership of the fund is a weak spot, but they invest in other ways. As of September 2018, Mitchell and Monahan each invested \$100,001-\$500,000 in the fund. That looks especially meager for the long-tenured Mitchell, but he and Monahan have directed some of their assets toward buying out retirees' stakes in the firm.

**Parent Pillar** + Positive | Tony Thomas, Ph.D. 10/08/2019

As a well-managed, investor-friendly boutique, Conestoga Capital Advisors earns a Positive Parent rating.

The small, employee-owned firm has handled successions well. Founded in 2001 by Bob Mitchell and Bill Martindale, it has been transparent when dealing with its few departures--all retirements. It used Martindale's 2014 retirement to let most of its dozen employees buy economic stakes in the business. This promotes firm longevity and strengthens employees' interests in the firm's success.

Conestoga's primary investment strategies are topnotch. It runs only two mutual funds, Conestoga Small Cap CCASX and Conestoga SMid-Cap CCSMX, which hold more than 60% of its \$4.7 billion in managed assets as of June 2019. Both have solid records and generous waivers that keep fees competitive. A tight-knit, five-member investment team uses clear and sensible parameters to build concentrated portfolios around profitable, low-debt companies.

Capacity management has been the toughest challenge, but the firm has been up to the task so far. The small-cap strategy's channel-by-channel closure in 2018 risked being too gradual to control asset growth, but flows subsided and the team kept the portfolio's attractive features intact. Capacity still bears watching, though, given the still-open smid-cap product's overlap with its small-cap sibling.

**Price Pillar** + Positive | Tony Thomas, Ph.D. 10/08/2019

Below-average fees earn this fund a Positive Price rating. The fund is closed to new investors.

Sizable fee waivers help keep investors' costs affordable. The firm caps operating expenses at 0.90% for the Institutional and 1.10% for the Investors share classes. That puts both expense ratios below the respective medians for similarly distributed shares (0.97% for institutional shares and 1.16% for no-load shares). The waivers are set to expire in January 2020, though the firm has indicated that it expects to renew them.

Total Returns % (As of 9/30/2019) <b>CONESTOGA SMALL CAP FUND</b>	Average Annualized Total Returns							
	QTD	YTD	1-Yr	3-Yr	5-Yr	7-Yr	10-Yr	Since Inception 10/1/2002
CCASX– Investors Class	-3.69	18.86	-3.57	17.26	15.73	14.75	14.70	12.23
Russell 2000® Growth Index	-4.17	15.34	-9.63	9.79	9.08	11.43	12.25	10.82
Russell 2000® Index	-2.40	14.18	-8.89	8.23	8.19	10.43	11.19	10.18

Gross expense ratio: 1.49%, Net expense ratio: 1.10%; Conestoga Capital Advisors, LLC (the Adviser) has contractually agreed to limit the Fund's net annual operating expenses to 1.10% of the Fund's average daily net assets until at least January 31, 2020, subject to termination at any time at the option of the Fund. There is no guarantee that the agreement to limit the Fund's annual operating expense will be renewed or extended.

*Performance is based upon closing NAV calculation on listed dates and represents past performance. Past performance does not guarantee future results and current performance may be lower or higher than the performance quoted. Performance data includes reinvestment of dividends. Investment returns and principal value of an investment in Conestoga Small Cap Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. For the Fund's daily NAV, list of additional holdings, total return as of the most recent month-end and a copy of the Fund's prospectus, please visit [www.conestogacapital.com](http://www.conestogacapital.com) or call 1-800-320-7790.*

Mutual Fund Investing involves risk, principal loss is possible. Investment in the Fund is subject to investment risks, including, without limitation, equity risk, market risk, management risk, small company risk, foreign investment risk, currency risk, large redemption risk. Funds that invest in small and mid-cap stocks are often more volatile than large cap stocks. Smaller companies generally face higher risks due to their limited product lines, markets and financial resources. For more information about the Fund, including the Fund's objectives, charges, expenses and risks (including more information about the risks listed above), please read the prospectus.

**An investor should consider investment objectives, risks, charges, and expenses carefully before investing. Download a prospectus, which contains this information or call toll free 1-800-494-2755. Read the prospectus carefully before investing or sending money.**

The Russell 2000 Growth Index measures the performance of those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values. An individual cannot invest directly in an index.

A rate of return (ROE) is the gain or loss on an investment over a specified time period, expressed as a percentage of the investment's cost. Gains on investments are defined as income received plus any capital gains realized on the sale of the investment.

Standard deviation is a measure of the dispersion of a set of data from its mean. If the data points are further from the mean, there is higher deviation within the data set. Standard deviation is calculated as the square root of variance by determining the variation between each data point relative to the mean.



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