

## U.S. Small Cap Growth Strategy

### Representative Commentary — 3Q25

| Performance                             | Annualized |        |        |       |       |        |
|---|------------|--------|--------|-------|-------|--------|
|   | 3Q25       | 1YR    | 3YR    | 5YR   | 7YR   | 10YR   |
| U.S. Small Cap Growth Composite (Gross) | 2.26%      | 7.84%  | 13.88% | 7.44% | 6.79% | 10.46% |
| U.S. Small Cap Growth Composite (Net)   | 2.01%      | 6.78%  | 12.76% | 6.38% | 5.73% | 9.38%  |
| Russell 2000® Growth Index              | 12.19%     | 13.56% | 16.67% | 8.41% | 6.61% | 9.90%  |

*Please see the important performance and other related disclosures at the end of this Commentary, which are an integral part of this quarterly Commentary Newsletter.*

In the third quarter, except for fixed income outside the U.S., all major assets classes had positive returns.

- Global economic activity measures lifted into expansion territory and solidly remained there (though U.S. metrics lagged the rest of the world).
- As widely expected, the U.S. Federal Reserve reduced its rates by 25 basis points in September while the Bank of England did so in August.
- Following Japanese Prime Minister Ishiba's resignation in September, the new PM appears poised to resurrect the past Abenomics of boosting investment and demand through stronger public-private partnerships.
  - That change may delay the Bank of Japan's prior intention to increase its rates.
- The global game of "tariff tit for tat" continued, adding greater-than-usual uncertainty and weighing on levels of consumer sentiment or confidence.

Equities continued their upward march with the U.S.'s Russell 3000® Index climbing 8%, ahead of the 5% return for the MSCI EAFE Index though lagging the 11% gain for the MSCI Emerging Markets Indexes.

- Risk was in favor this quarter with the highest factor returns from Beta and Residual Volatility in the U.S. and globally. There were also strong showings from Momentum in the U.S. and Earnings Variability ex-U.S.
  - Earnings Quality and Profitability were ignored or panned, indicating that companies with low accruals, stable fundamentals, and operating efficiencies were penalized.
  - That also was seen by the 17% return for the Russell Microcap Index, the best performance this quarter among the major indices.
- Within U.S. small and mid capitalization growth indexes, better returns came from stocks with zero or negative earnings.
  - That was especially pronounced for small cap growth where over 20% of the Russell 2000® Growth Index lacks positive earnings.
- There was also a broader preference for stocks with high beta or low returns on equity.

As our investment team meets with companies, dissects recent earnings reports, and reviews the global landscape, they note several dynamics in various market segments that guide our positioning:

- **AI remains a dominant theme**, though some cracks are beginning to appear. Industry participants questioned the pace of infrastructure spending to support AI – from semiconductors to industrial coolants – and how sustainable

that would be. Some of the spending appeared circular, such as NVIDIA committing billions of dollars to OpenAI only for the latter to reinvest a significant portion of that on the newest NVIDIA chips. With debt levels increasing for the biggest AI spenders, measures of capital spending-to-sales are approaching dot-com peak levels.

- In the near term, the AI fervor continued to **dampen enthusiasm for software** on perceptions that many application software uses will evaporate (from our recent visits to various user conferences, we saw continued strong demand for application software).
- Helped by a more accommodative Federal Reserve, **capital markets activities picked up**. There have been meaningful recoveries in the levels of M&A and IPOs in recent months.
- With the Federal Reserve poised to continue monetary easing, **Industrial segments rotated** away from secular areas, such as aerospace or HVAC, toward the cyclical areas of home builders or mining companies.

Amidst this environment, the portfolio trailed the Russell 2000® Growth Index in the third quarter.

Our preferences in the Consumer-oriented sectors lean toward value-oriented or specialty retailers, franchise models, premium brands, or support services for other consumer companies. One key contributor was **Pursuit Attractions**, an owner-operator of select lodgings and sightseeing at high-demand locations. We added to our position early in the quarter after Pursuit acquired a new property in Costa Rica, which tends to be a counter-cyclical market and seemed to be a good strategic fit. Later, the company's revenues and earnings both exceeded expectations. With several recent property acquisitions and strong forward bookings, Pursuit's management raised its guidance for the remainder of the year, which in turn propelled its shares up by 25%. The warehouse club operator **BJ's Wholesale** reported better-than-expected earnings though it had lower sales and weaker comparisons to prior periods (we thought that was well telegraphed). Management was also cautious with its forward guidance given the pressures on consumers, even as the company gained market share. BJ's has been making adjustments that we believe will be beneficial, but those can weigh on the stock price and limit our visibility in the short term. As its shares pulled back by -14% we also reduced our holdings.

Our preferences among Health Care stocks are those companies providing novel therapies for unmet needs that command premium pricing, or specialized service providers. One example was **NewAmsterdam Pharma**, a biopharma developer of cholesterol inhibitors for cardiovascular diseases. The company announced that several of its late-stage clinical trials were on track with additional positive data points reported. Its lead candidate, a CETP inhibitor, showed significant reductions in LDL levels without the adverse side effects seen with competing treatments. Combined, that elevated NewAmsterdam's shares by 57%. Climbing by 79% was **Merus**, a biopharma developer of immune-oncology treatments for certain tumors. At the start of the quarter, Merus's shares rose following positive clinical trial indications for its metastatic colorectal cancer treatment. At the end of the quarter, the company agreed to be acquired by a larger biopharma firm, Genmab A/S of Denmark. Offsetting that was a -38% partial quarter loss from **Inspire Medical Systems**, which develops medical equipment to treat obstructive sleep apnea. We had been optimistic about the rollout of its newest generation device, but Inspire had difficulty executing that earlier this year. Those problems persisted, so we exited the position. We felt differently about biopharma developer **Soleno Therapeutics** and added to our holdings as its shares pulled back by -19%. A short seller's report questioned the safety of Soleno's Vykat treatment for Prader-Willi Syndrome, a generic disorder leading to unnaturally intense and unsatiable hunger. We spoke with the company's management as well as academic clinicians and believe the bear case allegations are inaccurate or hyperbolic. Leaving the portfolio, though gaining 13% for the partial quarter, was **Verona Pharma**. In July, Merck announced plans to acquire this developer of treatments for allergic rhinitis and other chronic respiratory diseases, and we subsequently sold our shares. New to the strategy this quarter was **Mirum Pharmaceuticals**, a commercial-stage biopharma developer of liver disease treatments. Mirum is developing several new applications for its treatments, including expanding its flagship Livmarli to treat a third indication.

Many of our Industrials positions provide necessary business-to-business operational services, highly technical components, equipment enabling automation & efficiency improvements, or essential infrastructure services. A positive contributor to results was **Kratos Defense & Security**, the U.S. defense company producing unmanned systems and satellite communications. Early in the quarter, Kratos announced a new partnership with the German air force for its Valkyrie collaborative combat aircraft (CCA) and later noted that the Valkyrie CCA would become the program of record for the U.S. Marines. In its subsequent earnings report, Kratos's revenues, margins, and earnings all exceeded expectations with better-than-expected growth across all segments. Management noted several new high-probability wins at the end of its fiscal quarter, which should continue Kratos's sales momentum. In the near term, its shares gained 95% and we trimmed on that strength. **Casella Waste Systems** backed up by -18%. The solid waste handler's revenues were better than expected, but earnings were hampered by the slower-than-expected systems integration of newly acquired territories in Mid-Atlantic states and the implementation of a new enterprise resource planning system. We see both issues as transitory, knowing that

Casella in the past quickly improved margins of acquisitions and the ERP system should facilitate that, so we added to our position. Pulling back by -39% was **ACV Auctions**, the leading commercial digital marketplace for buying or selling used vehicles. Revenues and earnings were less than anticipated, stemming from a lower rate of listings converting to transactions. That seemed tied to broader macroeconomic concerns—which ACV previously highlighted—and temporary in nature. However, management erred on the side of caution by reducing its guidance for the rest of 2025, and we are reevaluating ACV’s place in the strategy. During the quarter we began a position in **UniFirst Corporation**, which supplies a range of work clothing, uniforms, protective apparel, and facility service products. Previously, UniFirst had less efficient operations than competitors, which led to relative underperformance. Over the last few years, UniFirst has made significant technological upgrades, enhancing both its operations and customer service. Those strategic improvements should improve its margins and benefit its share price.

Among the wide variety of Information Technology companies, we prefer critical system providers, specialized component designers, systems that improve productivity or efficiency for their clients, and others that are growing their shares of corporate IT budgets. Recently, short-term market sentiment penalized the secular growth area of software in favor of either cyclical semiconductors or anything related to the future possibility of quantum computing. In this environment, our general preference for application software companies showing steady demand became a headwind to our relative performance. An example of that was **Vertex, Inc.**, which provides end-to-end tax compliance software for large businesses. Vertex reported earnings that were slightly lower than expected because some of its enterprise contracts took longer to complete as some clients delayed signing with concerns about the macroeconomic environment. The elongated sales cycle pushed some revenues into later periods, though Vertex’s two-year targets remain intact. Still, Vertex’s shares were down -30% this quarter. Another challenge was **PAR Technology** and its -43% showing. A designer of software and hardware for the hospitality industry, PAR reported revenue and earnings that were in line with expectations, although its rate of annual recurring revenue slipped. This also seemed to be a case of clients cautious in their economic outlook and moving slower to sign or implement new contracts with PAR. The price change seemed like an overreaction and the company was near to closing several deals, though we want to see how that progresses in future quarters. Rebounding from weakness earlier in the year, contributing to results was the relatively new holding, **SiTime Corporation** that designs micro-electro-mechanical systems (MEMS) timing chips, such as oscillators and resonators, for electronic components. SiTime is the dominant market leader for MEMS timing chips, which are rapidly displacing quartz-based systems in high-performance processors. We initiated the position at the end of June and continued buying in July during SiTime’s share price weakness with a view that sales momentum from new design wins was accelerating. Subsequently, SiTime reported better-than-expected revenues and earnings that supported our evaluations, though when the initial price reaction was weak, we bought additional shares. Later in the quarter, as SiTime’s price increased by 39%, we trimmed back the position’s weight. Joining the strategy this quarter was **Mirion Technologies**, which manufactures radiation detection, measurement, and monitoring products serving nuclear power and medical applications. Its nuclear power solutions are used in over 95% of the world’s nuclear reactors while its medical products have a presence in 80% of the world’s cancer centers. The recent acquisition of Paragon Energy Solutions provides Mirion with additional safety-related offerings for nuclear power plants and provides Mirion with greater relevance to the small modular reactor (SMR) market via design wins with well-capitalized SMR manufacturers.

The preliminary indications from quarterly earnings reports show broader growth across economic sectors and size segments, with an additional tailwind of the typical end-of-year corporate budget spending flush. In the U.S., expectations remain high for an additional rate cut at the late-October FOMC meeting, but countering that optimism are the effects (as of this writing) of the Federal government shutdown over its budget impasse. Meanwhile, equity markets keep shrugging off negative news and searching for the next shiny new thing—recent hype surrounding quantum computing indicates that might be it. However, economic realities typically intrude on such halcyon views. Hence, we remain focused on the fundamentals, seeking those steady management teams capable of creating economic growth at their companies, which we believe will be rewarded over time by the markets. As always, we are available for any questions you might have.

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## **Firm and Composite Information**

*TimesSquare Capital Management, LLC ("TimesSquare") is a registered investment adviser that is owned by the former equity management team of TimesSquare Capital Management, Inc. ("TimesSquare Inc.") and Affiliated Managers Group, Inc. TimesSquare was formed to manage TimesSquare Inc.'s growth equity investment advisory business which was sold to TimesSquare in a transaction that closed on November 19, 2004. From October 1, 2000 to November 18, 2004, the performance is that of the TimesSquare Inc. small cap composite. From November 19, 2004, the performance is that of the TimesSquare small cap composite which consists of all small cap accounts managed by the team at TimesSquare and TimesSquare Inc. There has been no change in the investment management responsibility or strategy from the prior firm.*

*This composite invests in stocks with market capitalizations at time of purchase generally within the range of capitalizations of stocks in the Russell 2000 Growth Index. The process is fundamental research driven. The investment style is growth. Primary selection criteria include quality management, distinct competitive advantage, and strong, sustainable growth. Portfolios will hold approximately 90-120 stocks. Historical turnover has averaged 54% per year. Composite inclusion threshold \$5mm. Fee basis is 100 basis points. The composite creation and inception date is October 1, 2000.*

*From 04/01/2015 until 12/31/16, accounts are removed from the composites when significant cash flows occur. A significant cash flow is defined as an external flow that exceeds 10% of the composite's market value on the day of the cash flow. Effective January 1, 2017 this composite does not have a significant cash flow policy.*

*In July 2014, TimesSquare modified its purchase capitalization range to match the changes in the small cap market as represented by the Russell 2000® Growth Index. The purchase range was amended to reflect a range bounded by the approximate value of the smallest security in the index (in most cases) and the approximate value of 75% of the largest security's capitalization. These targets will be maintained for the subsequent 12 months, and may be adjusted based on the above rules each July following the reconstitution. In that manner, the targets would be responsive to higher or lower capitalization profiles of the indexes over time. Previously, in June 2012, TimesSquare had modified its purchase capitalization range to match the changes in the small cap market as represented by the Russell 2000® Growth Index at that time, with a change from \$50 million to \$1.5 billion at time of purchase to \$50 million to \$2 billion.*

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*TimesSquare's list of composites is available upon request. Past performance does not guarantee future results. The firm's list of limited distributed pooled funds are available upon request.*

## **Benchmark**

*Performance is measured against the Russell 2000® Growth – a market capitalization-weighted index that measures the performance of*

those Russell 2000® companies with higher price-to-book ratios and higher forecasted growth rates. All indexes, including the Russell 2000® Growth Index, are based on gross-of-fee returns. FTSE Russell is the source and owner of the Russell Index data contained or reflected in this material and all trademarks and copyrights related thereto. Benchmark returns are not covered by the report of independent verifiers.

### **Performance Calculations**

The performance figures shown are calculated in U.S. dollars on a size-weighted basis and reflect the reinvestment of dividends and other earnings, and the deduction of brokerage commissions and other transaction costs. Performance is provided on a gross basis (before the deduction of management fees) as well as net of the highest fee level from the standard fee schedule listed for this strategy during the period presented. Investment advisory fees generally charged by TimesSquare are described in Part 2A of its Form ADV. This composite may contain some accounts that have used performance based fees. To illustrate performance net of fees, assume \$20,000,000 is placed under management for ten years sustaining 10% compound gross total return. If an advisory fee of 1.00% of average assets under management is charged per year, for each year of the ten-year period, the resulting compound annual return would be reduced to 9.0%. The ending dollar value of the account would be \$47,347,274 compared with the unreduced account value of \$51,874,849.

Internal dispersion is calculated using the equal-weighted standard deviation of all accounts included in the composite on a gross basis for the entire year; it is not presented for periods less than one year or when there were five or fewer portfolios in the composite for the entire year.

The three-year annualized standard deviation measures the variability of the composite and the benchmark returns on a gross basis over the preceding 36-month period. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. To receive additional information regarding TimesSquare Capital Management, LLC, including a GIPS Composite Report for the strategy presented in this commentary, contact TimesSquare at [info@tscmlc.com](mailto:info@tscmlc.com).

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