



JUNE 30, 2023

CAMPBELL NEWMAN

# SMALL CAP GROWTH 2Q 2023 COMMENTARY

## MARKET OVERVIEW

While the Russell 2000 Growth Index (R2G) produced a strong quarterly return of 7.05%, Small Cap stocks continue to trail Large Caps, as seen in the Russell 1000 Growth Index's 2Q return of 12.81%. It was also another quarter of volatile returns, with negative performance through the first two months (likely a consequence of March's bank failures) but a robust 8.29% return in June.

Fueling the performance was a shift to a risk-on mentality, with June's rally led by the Energy, Industrials, Real Estate and Materials sectors -- all of which delivered double-digit returns. Another big theme during the quarter was the potential for rapid expansion of broad commercial applications for Generative AI, which contributed to the positive market sentiment. Other notable bright spots include spending on travel/leisure and housing, which points to a resilient consumer, despite the Fed's ongoing hawkish stance and its May rate increase to 5.00%-5.25%.

As noted, Large Caps generally outperformed Small Caps by style and Growth outperformed Value across market capitalizations. For example, the R2G's 7.05% return bested its Value counterpart by nearly 390 bps. This continues a trend seen in the first quarter, with the R2G's year-to-date return significantly outperforming the Russell 2000 Value (13.55% vs. 2.50%). Only two sectors outperformed the index, Health Care (13.14%) and Information Technology (7.56%), while two sectors reported negative performance, Utilities (-2.05%) and Materials (-0.08%).

## PORTFOLIO REVIEW

The Campbell Newman Small Cap Growth portfolio underperformed its Russell 2000 Growth benchmark with a gross return of 3.25% (3.06% net of fees) compared to 7.05%.



Stock selection in Consumer Discretionary was the greatest positive contributor to relative performance, adding 94 bps due to the portfolio sector return of 7.43% vs. the benchmark's 0.80%. Underweight exposure to the three worst performing sectors, Materials (1.92% weight vs. 4.49%), Communication Services (0.00% vs. 2.41%), and Utilities (0.00% vs. 1.70%), added 18 bps, 16 bps and 15 bps, respectively.

The greatest detractor to relative performance (220 bps) was stock selection in Health Care, with a portfolio return of 2.71% vs. 13.14% for the benchmark. Biotechnology was the Health Care sector's top performing industry, and the portfolio has little opportunity for exposure in Biotech due to the fact that 240 of its Index 255 constituents are unprofitable.

Stock selection in Financials cost 74 bps due to the portfolio's return of -7.68% vs. 2.72%. Stock selection in Information Technology cost another 72 bps with a portfolio return of 4.75% vs. 7.56%.

## TOP CONTRIBUTORS

**MasTec, Inc. (MAS)**, a diversified infrastructure specialty contractor, reported strong financial results with revenue growth of over 30%. All four business segments delivered growth, while backlog increased 7% relative to last quarter, with each business unit showing growth as strength remains broad based. With strong momentum and positive management comments on the prospects for growth in 2024, we remain positive on the investment story.

**Medpace Holdings, Inc. (MEDP)**, a global contract research organization providing Phase I-IV clinical development services to the biotechnology and pharma industries, reported a strong 31% increase in revenue in the quarter reflecting less funding challenges for its clients. Net new business awards were over \$555 million compared to \$423 million for the prior-year period. The company is increasing its revenue guidance for 2023 to \$1.8 billion, representing growth of 23%.

**Onto Innovation, Inc. (ONTO)**, a semiconductor capital equipment company focused on process control, exhibited strong stock price performance due to the emergence of artificial intelligence (AI) and the positive impact it will eventually have on demand. In addition, the number of AI servers, which account for about 5% of today's server units, should continue to grow meaningfully over time.

## BOTTOM CONTRIBUTORS

**MarketAxess Holdings, Inc. (MKTX)**, the operator of a leading electronic fixed-income trading platform, reported a good first quarter with a beat on both revenues and operating expenses. The stock has reacted negatively since the quarter due to a retracement in industry volumes resulting from the banking sector dislocation in March. We believe this is a temporary pause and continue to believe MKTX has a long runway for future growth as it gains market share in the high-yield and European markets.

**Ciena Corp. (CIEN)**, a leading provider of optical networking equipment, reported strong fiscal 2Q results though tempered its revenue outlook for the balance of the year. Due to a softer economic backdrop, customers have begun to push out order delivery into subsequent quarters as they scrutinize their budgets. Positively, CIEN's backlog is two times normal levels, representing roughly 50% of fiscal 2024 revenue forecasts. We remain confident in Ciena's growth prospects as it continues to benefit from 5G, cloud, automation and artificial intelligence.

**MP Materials Corp. (MP)**, the largest producer of rare earth materials in the Western Hemisphere, saw shares impacted as the price of rare earth commodities fell significantly with products MP is focused on finishing the quarter down nearly 40% from the start of the year. Importantly, MP is making progress on the transition from pure mining to eventual magnet production which will reduce the exposure to commodity movements. With strong execution, a cash-rich balance sheet and tailwinds from the electric vehicle transition, we continue to see MP as well positioned for the future.

## PORTFOLIO POSITIONING

The only change made during the quarter was the sale of the United Bankshares (UBSI) position, eliminating banking exposure from the portfolio due to the challenging industry outlook. Portfolio sector weights indicate where the team continues to find the greatest number of attractive longer-term investments. The portfolio continues to emphasize Information Technology (26.4% portfolio weight), Health Care (20.3%), Industrials (17.3%) and Consumer Discretionary (14.5%).



## TOP AND BOTTOM ABSOLUTE CONTRIBUTORS

2Q 2023 TOP CONTRIBUTORS	WEIGHT	RETURN (NET)	IMPACT (NET)
MasTec, Inc.	4.27%	24.91%	109 bps
Medpace Holdings, Inc.	3.63	27.71	93
Onto Innovation, Inc.	2.71	32.53	89
Century Communities, Inc.	2.60	20.30	52
Dycom Industries, Inc.	2.13	21.36	46

2Q 2023 BOTTOM CONTRIBUTORS	WEIGHT	RETURN (NET)	IMPACT (NET)
MarketAxess Holdings, Inc.	1.57%	-33.03%	-71 bps
Ciena Corp.	2.33	-19.10	-53
MP Materials Corp.	1.92	-18.84	-47
Integra Lifesciences Holdings Corp.	1.09	-28.36	-40
United Bankshares, Inc.	0.79	-15.82	-37

## PERFORMANCE

	2Q 2023	YTD 2023	1 YEAR	5 YEARS	ITD
Representative Account (Gross)	3.25%	8.65%	12.18%	8.90%	10.10%
Representative Account (Net)	3.06	8.28	11.46	8.29	9.53
Russell 2000 Growth Index	7.05	13.55	18.53	4.22	7.05

Returns greater than 1 year are annualized.

### IMPORTANT DISCLOSURES:

Past performance is not indicative of future results. All investments involve risk, including possible loss of principal. There is no guarantee investment objectives will be met. Gross returns are presented before deducting management fees (and custodian fees) and include the reinvestment of all income. Net returns are presented after the deduction of a model fee based on the highest fee paid then in effect for the period shown and include the reinvestment of all income. Performance returns are calculated using a time-weighted formula with appropriate adjustments for cash flows, and include all dividends and interest, accrued income, and realized and unrealized gains or losses. Indexes are unmanaged and do not incur fees or expenses. It is not possible to invest directly in an index. Portfolio sector weights reflect a representative account and are subject to change without notice. Sector returns are presented net of management fees. It should not be assumed that an investment in the sectors listed were, or will be, profitable. Portfolio holdings reflect a representative account and are subject to change. Other accounts within the strategy may have different holdings. Portfolio holdings should not be considered a recommendation to buy, hold or sell securities. Current and future portfolio holdings are subject to risk. Past performance does not guarantee future results. The future performance of any specific investment should not be assumed to be profitable or equal to past results. The performance of the holdings discussed above may have been the result of unique market circumstances that are no longer relevant. The holdings identified above do not represent all of the securities purchased, sold or recommended. Securities mentioned should not be construed as recommendation for purchase or sale. Portfolio transactions should not be considered a recommendation to buy, hold or sell securities.

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