TORRAY LLC
Investment management since 1972

TorrayResolute Concentrated Large Growth

Market Overview

The familiar phrase "expect the unexpected" is memorable in part because it makes no sense. Yet, this is exactly what we experienced and what we became accustomed to in 2016. The United Kingdom's decision to leave the European Union and the U.S. election of Donald Trump were considered long shots at best; outcomes uniformly expected to roil financial markets. Contrary to expectations, investors embraced change, or at least the promise of change, and pushed equity markets higher. The backdrop for this constructive, if unexpected response, was stable and improving economic fundamentals. As we move into the New Year, our focus is on how these changes might occur and their impact on the economy and markets.

Portfolio Commentary

The Large Growth Composite declined 2.01% (2.10% net of fees) for the fourth quarter, underperforming the benchmark's gain of 1.01%. While this was a moderately disappointing conclusion to the year, performance for the full year was good on an absolute and relative basis; the composite gained 7.25% (6.89% net of fees), keeping pace with the benchmark's gain of 7.08%, and finished in the top quartile of the Large Growth peer group.

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Security selection was the principal source of underperformance for the quarter, led lower by weakness in shares of healthcare information technology provider Cerner Corporation (CERN). The evolving regulatory environment and uncertainty associated with the presidential election tempered demand for the company's products and services. Over time, we expect the challenge of increasing healthcare productivity and the adoption of value-based reimbursement plans will stabilize and improve demand. Top detractors for the period also included LKQ Corp. (LKQ) and Facebook (FB). In contrast to the challenges faced by Cerner, shares of Charles Schwab (SCHW) and Akamai Technologies (AKAM) posted strong gains in excess of 25% for the quarter. Schwab continues to experience steady deposit growth, high earnings leverage to rising interest rates, and is expected to benefit from reduced regulations under the new administration. Akamai is experiencing accelerating growth and margin expansion as its Performance and Security division (59% of revenues) overtakes its commoditized Media Delivery division (34% of revenues). Financial services technology provider Fiserv (FISV) was also among the top contributors.

Despite the dynamic geopolitical backdrop, portfolio activity was modest for the period, with the initiation of a single new position and no outright sales during the quarter. We purchased shares of Acuity Brands (AYI), a designer and manufacturer of lighting equipment and associated building management solutions for commercial and residential applications. With revenues of $3.5 billion, Acuity holds the leading share position (18%) in the $19 billion North American lighting market. Acuity's early investment in efficient LED technologies, now 66% of revenues, enabled the company to secure exclusive distribution rights, forming the basis of its competitive advantage. We believe the healthy secular growth of approximately 30%-40% annually in LED fixtures, combined with market leadership and sustainable competitive advantages will support attractive rates of growth at Acuity for the next several years.

Outlook

There were two or three phases of the market in 2016, depending on how you count them; in the first half of the year, defensive stocks led cyclicals. In the second half, the trend reversed and cyclicals exploded higher post-election, with investors projecting that the Trump administration's business-friendly campaign platform of tax cuts, infrastructure spending and deregulation would bolster future economic activity. A frequent question we received prior to, and immediately following the election, was regarding the changes we had made to the portfolio in consideration of this event. As unsatisfactory as it may seem, our response was "none." While extraordinary events such as Brexit and the election of Donald Trump introduce risks and opportunities, it is, as we have been reminded this year, difficult to consistently predict the outcome of such events. We have evaluated the potential economic impact of the primary policy changes proposed by the new administration and believe the portfolio's risk exposure is balanced. As such, our approach to investing remains unchanged and balanced. As we look out to the New Year, we ask a question we expect many investors do: "Was 2016 a triumph of hope over reason or an inflection point for positive economic change?" We expect a bit of both.

As ever, we appreciate your interest and trust.

Nicholas Haffenreffer

Nicholas C. Haffenreffer
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Top Contributors & Detractors

Security	Sector	Contribution
Charles Schwab	Financials	+0.8
Akamai	Info Tech	+0.6
Fiserv	Info Tech	+0.3
United Technologies	Industrials	+0.3
Incyte	Health Care	+0.2
Cerner	Health Care	-0.8
LKQ Corporation	Cons Disc	-0.5
Facebook	Info Tech	-0.4
Hanesbrands	Cons Disc	-0.4
Colgate-Palmolive	Cons Stpls	-0.1

Top 10 Holdings

Security	% of Holdings
Alphabet	4.9
Charles Schwab	4.3
Fiserv	4.1
Apple	4.1
Visa	3.8
Facebook	3.8
LKQ Corporation	3.7
Danaher	3.6
Accenture	3.5
BioMarin	3.5
Percentage of total portfolio	**39.2**

Holdings are subject to change and are not recommendations to buy or sell a security.

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The Russell 1000® Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values.

Investing involves risk; principal loss is possible. Past performance is not indicative of future results.