TORRAY LLC

Investment management since 1972

TorrayResolute Concentrated Large Growth

The Market

2021 proved to be another good year for financial assets, with the broad S&P 500 Index returning 11% in the fourth quarter and 29% for the year. This Index has delivered strong positive returns in four out of the past five calendar years, and in 17 of the past 20 quarters (85% of the observations). The obvious question is "why have returns been so strong for so long?" and a related, more subtle question comes to mind, "does risk still matter?"

Over much of this period, the market has struggled with risk from a variety of sources, including COVID19, geopolitics, interest rates and inflation. Seemingly, the correct decision in response to each disruption was to buy and hold, especially the stocks of the largest companies. Profits and associated growth have driven these generally positive returns. The supportive economy has enjoyed robust demand and, more importantly, innovative, highly productive supply to meet this demand. Many of these new supply solutions are products and services that are leverageable, meaning new units can be quickly and cheaply brought to market. Think software, social media platforms and medical therapies that address unmet needs. In this context, inflation has remained low (until recently) which in turn supports expansionary interest rates. The market believes these favorable conditions will remain in place into the future. So, if this narrative holds, risk likely remains a secondary concern for many investors.

Composite Portfolio

The Large Cap Growth Composite ended the quarter and year with strong absolute returns of 10.51% (10.34% net of fees) and 27.48% (26.67% net of fees) respectively. Relative performance marginally lagged the primary benchmark over both time periods, as the Russell 1000 Growth Index returned 11.64% for the quarter and 27.60% for the year. The benchmark ended the year highly concentrated with nearly half of its value allocated to the information technology sector and over 20% in just two stocks, Apple (AAPL, up 34% in '21) and Microsoft (MSFT, up 53% in '21). When these do well, it is mathematically challenging for less concentrated active managers to outperform, which was certainly the case in 2021. For the quarter, the portfolio's top contributors were all technology stocks: Apple (AAPL), Microsoft (MSFT) and Accenture (ACN). Top detractors included Genmab (GMAB), Fiserv (FISV) and Visa (V).

In terms of trading, the quarter was a busy one. One stock, Roper Technologies (ROP), was sold, and two new investments were purchased, Entegris (ENTG) and Royalty Pharma (RPRX). ROP was eliminated because management is making changes we disagree with, most importantly the divestment of their tolling business, TransCore (a good source of recurring revenue). ENTG builds additional exposure to the semiconductor theme. They are a leader in consumable filters and chemicals used in the manufacturing process, both products that are essential to high yields and advanced designs. We think this is attractive because of the business's recurring nature and, hopefully, reduced cyclicality. RPRX, led by its founder and large shareholder, dominates the market for pharmaceutical and biotech royalties. A recent IPO, we are excited to invest as we have long admired the business model and management's track record since 1996. In our view, the industry has significant demand for capital to fund the next generation of medical therapies and royalties should increasingly be a major funding source supporting this goal.

Behavioral Finance

Returning to the question on risk, behavioral economists believe financial activities are influenced by irrational emotions instead of the rational decisions assumed by traditional 'efficient market' theory. Evidence from the great financial crisis of 2007/08 supports the behavioralists' conclusions, as efficient market models collapsed in a hard landing that destroyed trillions in paper wealth. This greed-and-fear dynamic suggests that markets follow emotional cycles, although the course is not readily predictable. If so, given where we currently are in the emotional cycle, after the extended period of positive returns, greed is a well-entrenched bias in today's financial arena. Small changes in the market's assessment of factors like growth, interest rates and justified valuations could have large implications for prices, as evident in market returns in the first few weeks of 2022. To us, this suggests risk should be a major consideration in portfolio construction.

Risk management has always been a hallmark of our strategies. The brutal math of recouping losses is what drives this emphasis. As we begin 2022, we remain focused on building portfolios of what we consider to be great businesses with favorable risk characteristics across the growth, value, and market capitalization spectrums.

As always, thank you for your business; please reach out any time with any issue.

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Q4 2021 Top Contributors & Detractors

Security	Sector	% Avg. Weight	% Contribution
Apple Inc.	Info Tech	6.1	+1.4
Microsoft Corporation	Info Tech	6.0	+1.1
Accenture Plc Class A	Info Tech	3.3	+0.9
Sherwin-Williams Company	Materials	3.2	+0.8
O'Reilly Automotive, Inc.	Cons Disc	4.1	+0.6
Genmab A/S Spons. ADR	Health Care	3.0	-0.3
Fiserv, Inc.	Info Tech	3.1	-0.1
Visa Inc. Class A	Info Tech	3.8	-0.1
Royalty Pharma Plc Class A	Health Care	0.9	-0.1
Meta Platforms Inc. Class A	Comm Services	3.2	-0.1

Q4 2021 Top 10 Holdings

Security	% Holdings
Apple Inc.	6.6
Alphabet Inc. Class A	6.2
Microsoft Corporation	6.0
Amazon.com, Inc.	5.6
O'Reilly Automotive, Inc.	4.4
American Tower Corp.	4.1
Visa Inc. Class A	3.9
Verisk Analytics Inc.	3.4
Adobe Inc.	3.4
Sherwin-Williams Company	3.4
Percentage of total portfolio	46.9

Holdings are subject to change and are not recommendations to buy or sell a security. To obtain information about the calculation methodology used to select the largest contributors to and detractors from performance or to obtain a list showing every holding's contribution to performance during the measurement period, contact bscalise@torray.com.

Source: FactSet and Torray LLC.