Quarterly commentary

As of September 30, 2020

Q3 2020 in Review Chiron SMid Opportunities Fund

The third quarter was positive for equities and credit, but there was a more global, more diversified feel to the return mix than has been the case in recent times. Asian equities led, followed closely by U.S. equities, with Europe and the U.K. experiencing more muted returns. The MSCI ACWI SMID Cap Index finished up 7.75% for the quarter and down -2.03% in September. The quarter started on a positive note as lockdown conditions were eased and we came out of a Q2 where we witnessed the largest decline in U.S. GDP since World War II. Investors were inundated with ongoing weak vs. encouraging data points and high frequency data in July and August, with the markets rumbling higher. As we entered September, to some the run felt extended, as evidenced by the uptick in volatility.

After the S&P 500 recorded an all-time high on September 2, the sell-off took hold. U.S. growth stocks, specifically tech names that had prospered with the stay-at-home tailwind, came under pressure. September finished with negative returns for both the S&P and Nasdaq. As measured by the VIX, volatility closed out the month at twice its average since the Global Financial Crisis. Though fixed income, as noted, was positive for the quarter, it offered little in the way of price appreciation or risk-off portfolio ballast amid the September sell-off. The U.S. dollar rose and gold was negative for September. Throughout the quarter, ISM readings were encouraging to the upside, housing was robust and employment continued to rebound, albeit at a slower pace than expected. The Federal Reserve's policy shift to average inflation targeting is intended to allow inflation to run above target to compensate for those times when it hasn't in the past. The takeaway is lower rates for the foreseeable future.

Elsewhere, European equities were slightly positive for the quarter but negative in September. COVID-19 cases picked up, especially in Spain, France and the U.K. The British pound moved down in September, reflecting the complications to Brexit caused by the U.K. government's introduction of the Internal Market Bill, which seeks to modify previously agreed-upon legislation and change trade between the U.K. and Northern Ireland. Emerging Markets led by China continued to see an acceleration in manufacturing activity as they have managed to return to near pre-pandemic population mobility numbers. Market participants are focused on the upcoming U.S. elections and the possible ramifications of victory for either party.

Q3 Fund Performance and Attribution Update

For the three months ending September 30, 2020, Chiron SMid Opportunities Fund (CSMOX) generated a total return of 9.68%, outperforming the MSCI ACWI SMID Cap Index (benchmark) return of 7.75%. By sector, Consumer Discretionary, Communication Services and Materials were the leading contributors to performance, while Energy and Consumer Staples detracted from performance. By country, the U.S., Australia and Germany had the largest positive contributions to performance, while Portugal detracted.

Portfolio Positioning

At the end of the third quarter, the Fund's top three sector weights were Consumer Discretionary at 21.2%, Industrials at 17.9% and Information Technology at 12.8%. Of the Fund's net asset value, 48.9% was invested in North America, 14.6% in Europe, 10.6% in Emerging Markets, 21.5% in Asia and 1.6% in the U.K.

We remain positioned for Value and global cyclicals. During the quarter, we increased our U.S. allocation while decreasing exposure to Asia, Europe, Emerging Markets and the U.K., although this was more a result of bottom-up security selection. By sector, we reduced our exposure to Industrials, Communication Services, Materials and Consumer Staples. We increased our weighting in Consumer Discretionary, Energy and Health Care, while Information Technology and Financials saw no change to their weight in the portfolio. By market cap, there was a slight decrease to Large Cap with the proceeds going to Mid and Small Cap.

Going Forward

At the end of the Q3, we were cyclically fully invested and likely won‘t get more aggressive from here—unless the market were to sell off, which would allow us to build some tactical positioning. Our Domain and Dispersion work is telling us not to get bearish, but to take risk. Lately, there has been some Small Cap and Value outperformance, which feels more real than in the past. Though the recovery is virus dependent and will not likely be smooth, we could be witnessing a bottoming-out of economic activity and believe that this could lead to smaller-cap outperformance over the intermediate term. It‘s possible we’re coming to the point where you would see that early-cycle handoff to small- and mid-cap stocks.

Looking forward, this is when we want to be aggressive and to embrace cheap, cyclical and international. Though we are not out of the woods yet, we believe that the fundamentals are better than GDP would suggest. The numbers won‘t be fantastic, but companies are getting a pass until things improve. If the economy rebounds quickly with the help of a vaccine, so much capacity has been cut that we could start to see more signs of inflation. If you are bullish about the pace of recovery, you will want to own cyclical Value. We will continue to look outside the U.S. in Emerging Markets, Europe and Japan given valuations, although there is cyclical Value to be found here as well. Extremely low rates and easy money have given many companies a pass on traditional fundamentals like margin expansion and cash flow production. We believe it is best to continue to build a portfolio based on these traditional pillars. Improving fundamentals will matter, and this is traditionally the time in the economic cycle when small- and mid-cap equities can start to have sustainable outperformance.

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