

# Timpani Small Cap Growth Strategy

# CALAMOS<sup>®</sup>

## INVESTMENTS

## Market Overview

U.S. equities saw strong gains during a volatile quarter. Equity price movements in May (to the downside) and June (to the upside) were greater on a percentage basis than the overall quarterly return for the S&P 500 Index, and the benchmark Russell 2000 Growth Index. Essentially, the U.S. equity market rallied in response to a more accommodative Fed policy outlook and lower bond yields. A seemingly positive, if not conclusive, meeting between the U.S. and China at the G20 Summit also lifted the general mood.

On the heels of a strong Q1 2019, stock prices continued to climb during Q2, but with additional volatility and overall market angst. The Federal Reserve held rates unchanged at its highly watched June meeting, and Chair Powell's remarks signaled a more dovish stance on future monetary policy actions. Market projections around Fed interest rate moves have changed dramatically since the start of the year and rate cuts are fully expected over the remainder of the year. Economic data has been mixed with generally better readings in consumption, services and employment, offset by slower growth in manufacturing, including industrial production and durable goods orders. Corporate earnings remain a mixed picture domestically, with year-over-growth only slightly positive

yet most companies beating estimates. Analysts are lowering expectations for second quarter earnings results based on lukewarm revenue growth and rising input costs. As mentioned, angst around global trade seemed to have eased as the U.S. and China appeared to make some progress and concessions, although no definitive agreements have been reached.

Growth stocks continued to lead, outperforming value stocks during the quarter. In terms of market cap, large and mid-cap stocks outperformed small caps for the quarter. While the broad market, as measured by the S&P 500 Index, was celebrating new all-time highs, small-cap stocks have yet to recoup prior highs. In our view, small caps and small-cap growth may have a good set up for initiating a catch-up phase relative to the broad market.

The Russell 2000 Growth Index was up 2.75% during the quarter. Despite gains in three of the past four quarters, the benchmark's 12-month return was relatively unchanged at -0.49%, owing mainly to the steep sell-off during Q4 2018 (-21.65%).

Investors continue to fret about the global and domestic economic outlook, providing a positive contrast for stocks that are able to show growth without macro tailwinds. This includes

**FIGURE 1. CALAMOS TIMPANI SMALL CAP GROWTH STRATEGY RETURNS**

	QTR ENDING 6/30/19	1-YEAR	3-YEAR	5-YEAR	10-YEAR	SINCE INCEPTION (4/08)
<b>Calamos Timpani Small Cap Growth Composite</b>						
Gross of Fees	6.21%	5.46%	23.10%	11.96%	17.44%	12.97%
Net of Fees	6.06	4.95	22.51	11.36	16.81	12.37
Russell 2000 Growth Index	2.75	-0.49	14.69	8.63	14.41	10.30

Source: Calamos Advisors LLC

Past performance is no guarantee of future results.

Data as of 6/30/19.

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**FIGURE 2. REPRESENTATIVE PORTFOLIO PERFORMANCE VERSUS RUSSELL 2000 GROWTH INDEX**  
SECOND QUARTER 2019

	CONTRIBUTORS (BPS)	DETRACTORS (BPS)
Health Care	239	
Consumer Discretionary	162	
Financials	74	
Energy	21	
Real Estate	10	
Information Technology	9	
Consumer Staples	5	
Utilities		-1
Materials		-3
Communication Services		-76
Industrials		-78

Attribution based on gross of fee performance with dividends reinvested. Performance attribution excludes any government/sovereign bonds or options on broad market indices the portfolio may hold.

Past performance is no guarantee of future results.

Source: Calamos Advisors LLC. Data as of 6/30/19.

many of the growth stocks in the Timpani portfolio. Therefore, we continue to be optimistic about our positioning.

## Performance Review

During the quarter, the portfolio delivered solid gains and outperformed the index due to better relative security selection. Many of the portfolio's holdings in higher-quality growth businesses performed well, as markets rewarded companies with leading fundamentals.

Analysis of the portfolio suggests stock selection drove positive relative performance, while sector allocation was modestly negative during the quarter. Regarding stock selection, health care, consumer discretionary and financials were the biggest contributors, while an underweight to the resurgent Industrials sector was the most significant detractor in terms of sector allocation. The allocation to communication services also weighed on return.

The biggest contributors to relative performance from a stock-specific basis were Strategic Education, Inc. and HEICO Corp.

Strategic Education operates within the education services industry of the Consumer Discretionary sector. With an emphasis on working adults, Strategic Education provides undergraduate and post-secondary education as well as non-degree training. While Strategic Education's stock has delivered strong performance throughout the year, shares saw a respectable increase during the quarter upon delivering better-than-expected results. Earnings were approximately 29% higher than the year-ago quarter, and higher enrollment as well as lower operating expenses were well received by the market. HEICO Corp. is an aerospace & defense company within the Industrials sector. HEICO designs, manufactures and sells products around the world to a range of customers including airlines, defense contractors, military agencies and NASA. During the quarter, HEICO announced net income gains of 37% year-over-year and a 20% gain in sales. Management raised guidance as well, noting strong demand across a variety of product lines.

2U, Inc. (*sold 06/19*), a worldwide provider of online educational services offering certification and degree programs, was the portfolio's biggest relative detractor for the quarter. During the quarter, 2U reported a loss. Although better than market expectations, the stock struggled on the day of announcement and over the second quarter after a strong first quarter. Management brought expectations down during the announcement, which weighed heavily on investor sentiment. Glu Mobile, Inc. (*sold 07/19*), an interactive home entertainment company within the communications services sector, also underperformed during the quarter and was a detractor. Glu Mobile develops and publishes mobile games for smartphone and tablet users, offering its own branded games in addition to third-party licenses. Glu Mobile's stock sold off in May on the heels of mixed results. Quarterly and yearly revenues were strong, but profits and forward guidance disappointed.

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**FIGURE 3. SECTOR ALLOCATIONS VERSUS RUSSELL 2000 GROWTH INDEX**

SECTOR	REPRESENTATIVE PORTFOLIO %	RUSSELL 2000 GROWTH INDEX%	UNDER/OVERWEIGHT %
Health Care	29.7	26.5	3.2
Information Technology	24.4	18.5	5.8
Consumer Discretionary	23.5	14.7	8.9
Industrials	8.3	18.6	-10.3
Financials	5.1	7.1	-2.0
Materials	2.8	3.3	-0.5
Consumer Staples	2.7	2.9	-0.2
Energy	2.5	1.7	0.8
Communication Services	1.2	3.1	-1.9
Real Estate	0.0	3.2	-3.2
Utilities	0.0	0.5	-0.5

This strategy is actively managed. Holdings, weightings and allocations are subject to change daily. Sector weightings exclude cash or cash equivalents, any government/sovereign bonds or broad-based index hedging securities/options the portfolio may hold. Sector allocations in table are based on end weights, while commentary weightings can be based on average weights. Therefore, the sector allocations table and commentary text may reference different sector assignments.

Source: Calamos Advisors LLC. Data as of 6/30/19.

## Positioning and Portfolio Changes

Regarding sector positioning, we ended the quarter with notable overweight positions in consumer discretionary and information technology countered by underweights in real estate and utilities. The underweights represent sectors where we have no holdings as of quarter end and represent small segments for the growth benchmark. The portfolio remains tilted toward secular growth stocks that are less dependent on the growth of the overall economy. We believe this is especially prudent now given the pervading macroeconomic murkiness and strong likelihood that the overall economy is facing a low-growth environment.

## Outlook

While headline risks rotated from topic to topic and investor sentiment varied strongly during the quarter, our views have not changed as dramatically. Domestic and international economic sluggishness remain at the forefront of market concerns. Domestically, market bears are focused on decelerating earnings growth rates and parts of the bond yield curve inverting, which

may be a leading indicator of recession. Bulls counter, saying the earnings growth deceleration is mainly due to difficult comparisons made more ambiguous by macro factors such as corporate tax reform and the yield curve inversion, which is only partial and may not lead to a recession near-term. We lean bullish and continue to believe we are likely several quarters away from a recession. For the next several quarters, we believe the most likely scenario is a low-growth, non-recessionary economic environment. Because of the scarcity of growth, this backdrop should enhance valuations for secular growth stocks overall, including those in Timpani's portfolio.

In summary, we are optimistic about the portfolio's prospects and remain committed to our long-term approach of investing in companies with fundamental momentum. We seek companies with a sustained, underestimated growth profile and overlay that approach with an unemotional, value-added sell discipline. We believe this process creates the most value for our clients and mutual fund shareholders over time.

# Calamos Timpani Small Cap Growth Strategy

Past performance does not guarantee or indicate future results. Current performance may be lower or higher than the performance quoted. Portfolios are managed according to their respective strategies which may differ significantly in terms of security holdings, industry weightings, and asset allocation from those of the benchmark(s). Portfolio performance, characteristics and volatility may differ from the benchmark(s) shown.

The results portrayed on the preceding pages are for the Calamos Timpani Small Cap Growth Composite. Representative holdings and portfolio characteristics are specific only to the portfolio shown at that point in time. Other portfolios will vary in composition, characteristics, and will experience different investment results. The representative portfolio shown has been selected by the advisor based on account characteristics that the advisor feels accurately represents the investment strategy as a whole.

Returns reflect the Calamos Timpani Small Cap Growth Composite, which is an actively managed Composite investing in common stocks of small market capitalization companies with sound growth potential. The Composite was created June 1, 2019, and calculated with an inception date of April 1, 2008. Results include all fully discretionary accounts, including those no longer with the Firm. Past performance is no guarantee of future results. On May 31, 2019, Calamos acquired Timpani Capital Management LLC, which has managed the strategy since its inception in 2008. All returns are net of commission and other similar fees charged on securities transactions and include reinvestment of net realized gains and interest.

Fees include the investment advisory fee charge by Calamos Advisors LLC. Returns greater than 12 months are annualized. Chart Data

Sources: Mellon Analytical Solutions LLC and Calamos Advisors LLC.

The primary benchmark is the Russell 2000® Growth Index. The Russell 2000 Growth Index measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000 companies with higher price-to-value ratios and higher forecasted growth values. The Russell 2000 Growth Index is published and maintained by FTSE Russell. Unmanaged index returns assume reinvestment of any and all distributions and do not reflect any fees, expenses or sales charges. Investors cannot invest directly in an index.

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