



## Philosophy

Fort Washington believes that there are inefficiencies in the small cap growth market. To capitalize on these, we focus on companies that are experiencing improving secular or cyclical fundamental trends, companies that are of high quality and well-managed, and companies with competitive business models.

## Process

Fort Washington's Small Cap Growth Equity strategy is based on a disciplined bottom-up process emphasizing stock selection along with consideration of industry exposure. Our stock selection process uses proprietary quantitative ranking tools to provide a "bullpen" of ideas on the best small cap growth securities. Sector specialists focus on companies with improving fundamentals that are favorably positioned to form sustainable competitive advantages within their industries. The target market cap range is \$100 million to \$2.5 billion. Risk is also controlled by limiting sector weights to approximately +/-5% around the Russell 2000 Growth Index.

## Investment Professionals

### Richard R. Jandrain III

Managing Director  
Senior Portfolio Manager  
Sector: Technology  
33 Years Experience

### Daniel J. Kapusta

Senior Portfolio Manager  
Sectors: Consumer & Finance  
(Brokers & REITs)  
23 Years Experience

### David K. Robinson, CFA

Senior Portfolio Manager  
Sectors: Industrial, Materials, & Energy  
24 Years Experience

### Bihag N. Patel, CFA

Senior Portfolio Manager  
Sectors: Healthcare & Finance  
(Insurance & Banks)  
12 Years Experience

## Performance

While the Small Cap Growth strategy composite declined in Q2 2010, it modestly outperformed its benchmark index, the Russell 2000 Growth.

## Factors Contributing to Performance

The consumer discretionary, financials and energy sectors had the most positive relative impact on returns in the quarter. Poor performance in the industrial and healthcare sectors detracted from performance. Continued strength in our value-based entertainment theme in consumer, strong earnings announcements from the companies in our debt collection theme within financials, and a takeover in tech were all drivers of strong individual stock returns in the quarter. Stocks that hurt the portfolio were driven by weak earnings reports/guidance and some company specific issues negatively impacted several healthcare names.

## Market Review

After over 13 months of nearly uninterrupted appreciation in the equity markets, concerns in May and June about European sovereign debt and a slowdown in the global economy injected volatility back into the markets. Yet the second quarter of 2010 began on the same note as the prior one year - very strong. The benchmark Russell 2000 Growth Index was up approximately 7% in the first three weeks of April, adding to its already impressive gains from the lows of March of 2009. However, in late April, renewed concerns about several European countries' government debt, namely Greece, Spain and others, caused sentiment to change quickly and the Russell 2000 Growth declined nearly 6% in just seven trading sessions between late April and early May. Trading on May 7th intensified investor fears even further as the so-called "flash crash" occurred and the Dow Jones Industrial Average at one point in the afternoon had declined nearly 1000 points for the session, and most of that in a matter of minutes, before rallying toward the close.

On the economic front, several factors have created some uneasiness about the strength of the global recovery including 1) China's efforts to modestly slow its economy, 2) anticipated slowing in Europe due to debt concerns and 3) some moderating to negative economic reports in the U.S. The question is if these numbers indicate a mere slowing from what appeared to be very strong economic reports over the prior few months and quarters or whether it portends a more troublesome deterioration which could lead to a double dip recession. In the US, the May jobs numbers as well as several weeks of poor unemployment claims continue to show the labor market is challenged. Also, softer than expected GDP, retail, manufacturing, and consumer confidence numbers have shown the economy is likely slowing. How much is yet to be determined.

## Portfolio Positioning and Outlook

The portfolio is positioned as follows:

As of the end of Q2 2010, the portfolio's largest sector overweight is in consumer discretionary (nearly 4% over the index sector weight). We also have roughly 2.5% overweight positions in healthcare and financials.

- Although we are toward the high end of our maximum overweight in consumer discretionary, our holdings are generally focused on the companies that serve value-conscious consumers and/or have strong organic top line growth driven by domestic geographic expansion, international growth and/or recurring revenue.
- In healthcare, our theme is in orphan-drug producers, and device manufacturers with new product introductions.
- Our overweight in financials is driven largely by holdings in pawn brokers and debt collection companies, which should benefited from the continued contraction in consumer credit, higher gold prices and increasing supply of charged off credit card debt.
- Our largest underweights are in industrials (-5%), consumer staples (-3%) and materials (-2.5%). In industrials and materials, we believe that because of a potential slowing of the global economy, and potentially even in China, these sectors will be more challenged. In consumer staples, we have chosen to redeploy those funds into companies in consumer discretionary that we believe have more growth potential but have somewhat defensive characteristics similar to staple names.

## Small Cap Growth

- Lastly, we are roughly equally weighted in technology and are positioned in companies that we believe will benefit from the need for increased data capacity in both internet and wireless applications.

As was mentioned earlier, the economy appears to be slowing modestly. Some of that slowing is to be expected as inventories are replenished from their extremely low levels. Once inventories are more in line with end demand, that positive driver to earnings will wane. Corporate cost-saving initiatives put in place a year ago that have driven significant earnings improvement will continue to help but at a moderating pace. Also the May and June payroll reports have highlighted the continued struggles of the labor market. Because of the reasons highlighted we are still somewhat cautious as it appears that robust economic growth may not be likely in the near term. Thus our focus is on finding companies that have the ability to increase sales even in a difficult economic environment. In addition, companies that can improve operating margins and generate EPS growth in the absence of top line growth will be considered if they provide sustainable margin expansion, strong cash flow metrics and returns on capital as well as solid balance sheets.

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