# Adirondack Small Cap Fund (ADKSX)

**Data as of March 31, 2020**

## Quarterly Commentary

Dear Fellow Shareholders,

First and foremost, we hope everyone is healthy and safe. The COVID-19 outbreak made for an extremely challenging environment for all risk assets during the first quarter of 2020. The world experienced a public health crisis that rapidly moved from a dangerous but presumably, containable outbreak into a global pandemic. As we write this update, the Governor of New York extended the lockdown until May 15 and signed an executive order requiring face masks in public when social distancing is not possible. On a positive note COVID-19 cases appear to be leveling off, a sign that extreme social distancing measures are working.

The market reaction to a near-global economic shutdown has been swift and unprecedented. During the quarter ending March 31, 2020, The Adirondack Small Cap Fund (ADKSX) declined by 36.3%. Over the same period, its benchmark, the Russell 2000® Value Index (RUJ), decreased by 35.7%. Fortunately, this economic shock has been met with extraordinary monetary and fiscal stimulus measures to cushion the blow. Since those measures were taken, credit markets are functioning better and the market has bounced, though much remains to be sorted out. The Fund's annualized return for 1 year, 5 year, and 10 year was (36.07)%, (7.51%), and 2.94%, respectively.*

Our prevailing strategy during this crisis has been to carefully move up the size and quality spectrum while reducing exposure to turnaround situations. We are focusing on allocating capital to those companies that could weather a severe recession, we need to be mindful, however, that "Quality" and "Defense" are crowded trades at this moment. Many active managers who played defense during the last recession were left behind when stocks recovered unexpectedly in 2009. In these uncertain times, we are thoroughly assessing the capacity of companies and industries within the portfolio to endure lower revenue, slower inventory turnover, and potentially extended collections. For example, we exited the Fund's position in JetBlue (JBLU). The outlook for air travel is murky at best and while government assistance is likely, the level of such support is still unclear. We still believe that people will continue to prefer experiences over possessions, and will closely follow the experience space for signs of recovery. As contrarians, we hardly need persuasion that travel and leisure will once again offer incredible investment opportunities, but until the smoke clears we will remain on the sidelines.

We are also keen on adding exposure to companies whose Officers or Directors have accumulated shares during the market meltdown. For instance, Charles Fabrikant, CEO of SEACOR Holding's (CKH) added to his holdings in early March for the first time in more than a decade. Fabrikant does not hold quarterly conference calls and shuns publicity but has a long history of shrewd investments, earning him the nickname "The best CEO nobody has ever heard of". SEACOR focuses on shipping/logistics primarily within North America and the Caribbean. While shipping/logistics is notoriously cyclical, much of their focus is on the transportation of food and agricultural products. SEACOR also ships government cargos that support more than 250,000 military servicemembers around the world. We continue to take advantage of market volatility to add to the funds SEACOR Holding's position. (as of 3/31/2020, CKH represented 1.78% of the portfolio.)

We made some changes to the fund's energy exposure. We exited two exploration and production investments challenged by the dramatic drop in oil/liquids prices (Callon Petroleum (CPE) and Southwest Energy (SWN)). Instead, we added Cabot Oil & Gas Corp (COG .84%) the strongest and lowest cost independent natural gas producer in the United States. (as of 3/31/2020, COG represented 0.84% of the portfolio.) There are a number of factors that should benefit U.S. natural gas prices going forward. Most important for gas is the substantial U.S. based export capacity that continues to come online. It is also important to note that over half of the Fund's energy exposure is now concentrated in shipping which often benefits from lower-priced oil. We think oil prices will recover slowly and that could result in many restructurings in the energy sector.

**Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Fund may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 888-686-2729, or visiting www.adirondackfunds.com.*

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Over the past six months, the Fund has returned to a considerable overweight in technology which on March 31st was 23.3% versus 11.4% for the index (RUJ). The Fund's current technology weighting is slightly above the Fund's historical average of approximately 20%. We added a new name in technology, Unisys Corp (UIS), largely because they completed a major deleveraging transaction which significantly improves their appeal to both prospective clients and shareholders (as of 3/31/2020, UIS represented 3.74% of the portfolio). The balance of the Fund's technology exposure includes companies serving in mission-critical areas such as 5G equipment, Business Process Outsourcing, Streaming Networks, Software and Communications services.

We trimmed the Fund's exposure to financial services from 23.3% for the quarter ending 12/31/19 to 21.2% for the quarter ending 3/31/20 and are still considerably lower than the benchmark (RUJ) at 29.9% as of 3/31/20. We sold out of shares of Brookline Bancorp Inc. (BRKL) which was the Fund's only bank stock. In 2008/09 the banks received direct financial support from Treasury and the credit issues were largely contained within residential mortgage and home equity lending. The current crisis, however, will likely present challenges for both commercial and consumer loans, thus making it far more difficult for investors to handicap. We believe smaller and midsized banks lack the earnings power of their larger peers and will struggle until credit issues are quantified and employment is seen as moving in the right direction. We screened for insider buying within the small-cap population of 343 banks during March and found only a few instances where insiders acquired meaningful ($150,000 or more) shares of stock during this severe correction. Another data point convincing us to steer clear of the banks for the moment.

These are unusual times. Money has flooded into treasuries driving the interest rate on the 30-year bond down from the low 2% range to the low 1% range, despite the looming prospect for enormous stimulus borrowing causing inflation. Even a modest upward move in rates could inflict significant capital "losses" on government debt holders if we have an unexpected uptick in economic activity. The potential for inflation is not a consensus call, but tighter credit and the lack of capital going into the materials and energy sectors could be problematic for input prices going forward. Especially if we have a sudden and sharp rise in commerce once the shutdown is lifted. The first quarter of 2020 saw the largest quarterly decline on record for the Russell 2000 value index and the worst relative performance to the S&P 500. History has shown that outperformance often (not always) follows periods of extreme underperformance. Small Cap Value now trades the largest discount to Small-Cap Growth on record. Our conviction in the portfolio is the strongest it has been since the 2008 recession. All employees of the Fund's advisor (Adirondack Research and Management) purchased shares of the Fund during the quarter. We expect more volatility in the near-term but believe the portfolio is well-positioned to endure the challenging times ahead.

The courage and compassion of those frontline healthcare workers should serve as a lesson to us all. Today's challenges will likely yield numerous innovations and greatly advance our understanding of infectious diseases. We at Adirondack and our service providers have been operating normally while utilizing some of our business continuity plans capabilities to comply with social distancing mandates. We are healthy and following the advice of experts to protect the safety of our families and our community. We hope that you and your family continue to stay safe and healthy during the challenging months ahead. We thank you for your continued support and investment. We look forward to better days ahead. For the most up-to-date information on your investment, please visit our website at www.adirondackfunds.com or call us at (518) 690-0470.

Regards,

Matt Reiner, CFA®
Portfolio Manager

Greg Roeder, CFA®
Portfolio Manager

Per the prospectus, the Fund's gross annual operating expense ratio is 1.24%. The Advisor has contractually agreed to waive fees or reimburse the Fund to the extent necessary to maintain the Fund's total annual operating expenses at 1.48% until August 1, 2020, subject to termination by the Fund on 60 days' *written notice.*

*The Fund invests in smaller companies, which involve additional risks such as limited liquidity and greater volatility. Additionally, value investing is subject to the risk that a company's intrinsic value may never be fully realized by the market.*

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*The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and it may be obtained by calling 1-888-686-2729, or visiting www.adirondackfunds.com. Read it carefully before investing. The Adirondack Small Cap Fund is distributed by Rafferty Capital Markets, LLC, Garden City, NY 11530.*

*The Russell 2000 Value Index measures the performance of small-cap value segment of the U.S. equity universe. It includes those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values. You cannot invest directly in an index.*

*Treasuries are one of four types of debt (bills, notes, bonds, and Inflation-Protected Securities) issued by the United States Department of the Treasury to finance U.S. government expenses.*

*The S&P 500 Index is a market value-weighted index of 500 stocks seen as indicators of U.S. equities and reflects large cap performance. You cannot invest directly in an index.*

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