

# Adirondack Small Cap Fund (ADKSX)

Data as of December 31, 2020

## Quarterly Commentary

Dear Fellow Shareholder,

During the quarter ended December 31, 2020, The Adirondack Small Cap Fund (ADKSX) generated returns of 35.46%. Over the same period, its benchmark, the Russell 2000® Value Index (RUJ), increased 33.36%. The Fund's annualized return for 1 year, 5 year, and 10 year was 5.29%, 4.34%, and 6.25%, respectively.\* The top ten holdings represented 37.8% of Fund assets, in line with our objective to focus on our best ideas. Portfolio turnover for the year ending 12/31/2020 was 36.8%.

The final stretch of the year, the fourth quarter, is typically known for more excitement than earlier ones. This is usually characterized by increased volatility as election results, holiday spending and yearend portfolio balancing can combine to have strong influence on the markets. Last quarter began with more than the typical collection of worries for investors. A consequential U.S. election, for both executive and legislative branches of government, Brexit in Europe, China trade tensions, more lockdowns, vaccine uncertainty, and ambiguity around stimulus were all influences on the market during the fourth quarter. Yet the market powered through these worries, and the small-cap segment posted its best fourth quarter ever.

Small-cap value returns were propelled by the Financial, Technology, Energy, and Materials sectors. Digging deeper, low-quality stocks (low share price, highly shorted, unprofitable) helped boost index (RUJ) performance. ADKSX benefited from being overweight Technology while also having winning picks in Healthcare and Consumer Discretionary. ODP Corp (as of 12/31/2020 ODP represented 2.38% of the portfolio) and Under Armour Inc. (as of 12/31/2020 UAA represented 2.01% of the portfolio) reported earnings that considerably exceeded analyst's estimates. Within healthcare, Allscripts Healthcare Solutions Inc.'s (as of 12/31/2020 MDRX represented 4.32% of the portfolio) intention to return significant cash to shareholders resulting from the sale of assets was cheered by investors. Accuray Inc. (as of 12/31/2020 ARAY represented 1.77% of the portfolio), a radiation therapy manufacturer, benefitted from its joint venture in China.

Most everything started to work in small caps once the Covid-19 vaccine moved from laboratories into the arms of front-line healthcare workers. Credit conditions continue to be lenient, and for the most part, companies handily beat earnings expectations. Within The Adirondack Small Cap Fund portfolio, more than half the companies held exceeded earnings estimates by more than 25%. While the bar set by analysts covering these companies was relatively low, we were still encouraged by their performance in challenging conditions.

We are pleased with Q4 relative performance as we continue to upgrade the portfolio to encounter what we view as formidable economic challenges going forward. We remain focused on better balance sheets and earnings quality, while avoiding the casino like speculations and lower quality entities that have been driven to extreme valuations by the Robinhood and Reddit crowd. The trend lately for these speculators has been to trade smaller stocks where they collectively have a greater impact on prices. Penny stocks, micro-caps, and small-caps are all fair game. During Q4 we saw evidence of such speculation, and more could follow, but we are certain that this casino like activity will end badly for those involved. We believe that their impact on small-cap benchmarks will be short-lived.

There is a growing notion that professional investors who managed money through the 1999/2000 bubble and through the 2008/2009 crisis, don't understand this new world. Instead, novice investors that have never bothered to read a 10K, model future cash flows, assess competitive issues, consider regulatory threats and review entry barriers are somehow better predictors of the future. Naturally, we don't buy into this reasoning. Grounded in our discipline is the central tenet that the long-term value of a firm is the sum discounted value of future cash flows and based on thoughtful assumptions concerning its cost of capital and competitive position.

*\*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](http://www.adirondackfunds.com).*

*Per the prospectus, the Fund's gross annual operating expense ratio is 1.36%. 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, 2021, subject to termination by the Fund on 60 days' written notice.*

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## Quarterly Commentary (con't)

So, where do we go from here? While a handful of measures show small-caps (both value and growth) to be overbought and possibly due for consolidation, the gap between value and growth remains historically wide. Small-caps have bounced hard off the March bottom, putting this asset class far ahead of historical norms. Normally it takes a year and a half for small-caps to post-performance similar to what we have seen since March. The differentiating factor measured against past markets is the astonishingly low rates fostered by massive stimulus and quantitative easing. The 10-year Treasury Note yield is currently hovering near 1.0%, and inflation as measured by the Consumer Price Index was up 1.4% in 2020 (12-month percent change in the Consumer Price Index for all Urban Consumers, selected items, not seasonally adjusted). It's hard for stocks (especially small-cap value) to look relatively expensive as compared to fixed income in this negative real rate environment. After a stellar performance in Q4, per Bloomberg/Morningstar small-cap value trades at 18x earnings, 2.02% dividend yield, with 4.83% annual earnings growth (2015-2020). As of year-end, per Bloomberg/Morningstar, assets in money market funds were still above levels seen in March when stocks were down -30%, suggesting that this rally has not been universally embraced. If funds on the sidelines find their way into the market, we could see further appreciation.

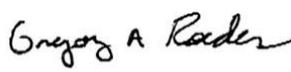
It's no secret that active management is maligned right now, but rest assured that at no time in the past 20 years has the need for active management been more crucial. When odd behavioral motivations push stocks to extremes, the next inevitable move for assets will be from the undisciplined, poorly informed stock flippers (indexes and novice investors) to patient, informed, and methodical investors. We believe our best days are coming, and we are confident that there will be more fantastic companies that will need investors who think like owners.

Finally, we would like to take this opportunity to thank you for your trust in our team. We intend to continue carefully managing your capital through these increasingly complex and challenging times. Best wishes for a happy and healthy new year. For the most up-to-date information on your investment, please visit our website at [www.adirondackfunds.com](http://www.adirondackfunds.com) or call us at (518) 690-0470.

Regards,



Matt Reiner, CFA®  
Portfolio Manager



Greg Roeder, CFA®  
Portfolio Manager

*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.*

*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](http://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.*

*Portfolio turnover is a measure of how frequently assets within a fund are bought and sold.*

*The 10-year Treasury Note is a debt obligation issued by the United States government. It has a maturity of 10 years upon initial issuance (paying the face value at maturity to the holder) and pays interest at a fixed rate once every six months.*

*Consumer Price Index (CPI) measures the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Indexes are available for the United States and other geographic areas.*