Argent Capital Management LLC

Small Cap Core Commentary – Fourth Quarter 2019

Some of you may have attended Argent's December Market Outlook luncheon this year. During the presentation, we discussed "unicorns". We weren't referring to a mythical creature with a single horn, but, instead, a name that Wall Street has coined for start-up companies with valuations, believe it or not, of over one billion dollars. Many of these "unicorn" companies are going public with virtually no earnings or positive cash flow; think companies like Uber, Lyft and Wayfair. Most of these companies went public feeling the market would offer a high stock price, not a valuation based on company fundamentals or strong earnings, but on the *possibility* of growth. Now, investors are starting to show concern with these unprofitable companies. Investors are once again remembering that profitable companies generally make the best investments.

Argent's Change-Based[SM] investment process looks for companies that are undergoing positive change with the expectation that this change will drive revenue and earnings growth rates higher. As part of that process, "unicorns" are frequently passed given these companies are not focused on earnings and cash flow – we are. The market's recent shift back to an emphasis on earnings and cash flow has been favorable to the Argent investment process.

In the world of small cap companies we see many "unicorn" type companies in one sector in particular, healthcare. At times, we are asked by clients why we don't own more pharmaceutical and biotechnology companies in the Argent Small Cap strategy. The answer goes back to Argent's investment process. A large number of companies in these two groups do not yet have a product to sell. Instead, they typically spend more than they earn because a product is still in trials - trying to prove their new drug or technology will be effective. Investors obviously have difficulty assigning a value to that, and that is why we tend to stay on the sidelines until there are traditional fundamental benchmarks of earnings and cash flow to review and analyze.

One example of a healthcare company that *does* meet the criteria of our investment process is Omnicell, Inc. Founded in 1992, Omnicell offers pharmacy solutions, manufacturing medication dispensing systems, pharmacy inventory management systems and related software solutions primarily for hospitals in the United States and Canada. Healthcare demographics in the United States is trending toward more medications. These medications need to be managed through the cycle of manufacturing, distribution to pharmacies and medications dispensed in hospitals. Omnicell has an interesting business model because they are developing solutions that reduce the level of human error when managing and dispensing these medications.

We have four successful equity strategies – Large Cap U.S., Small Cap U.S., Dividend Select and Mid Cap U.S. If you have questions about any of these options or know others who might have an interest in our strategies, please call us.

Sincerely,

Eddie Vigil

Eddie Vigil
Portfolio Manager