

Wasatch Core Growth Fund

MARCH 31, 2024

Positioning the Portfolio Amid AI Hype and Reality

OVERVIEW

The Wasatch Core Growth Fund—Investor Class gained 4.46% for the first quarter but underperformed the benchmark Russell 2000® Growth Index, which rose 7.58%. The broader Russell 2000 Index increased 5.18%. Among sectors, our performance in health care, industrials and consumer staples—and our zero weights in utilities and communication services—contributed to Fund performance relative to the benchmark. Conversely, our holdings in information technology, financials and consumer discretionary underperformed their benchmark counterparts.

Recently, the financial press has widely reported on the importance of the “Magnificent Seven” tech companies and their dominance in large-cap indexes. The main reason has been the companies’ progress in creating the software and hardware needed for artificial intelligence (AI).

But AI and technology more broadly have driven small-cap indexes too. In this regard, consider the Russell 2000 Growth Index and the 11 sectors that comprise it. The Index itself was up 7.58% for the first quarter. The information-technology sector (IT), which has a weight of nearly 23%, was up approximately 16%. The other 10 sectors were up about 5% overall. In other words, information technology produced approximately half of the Index’s total return. Moreover, omitting just the

FUND MANAGERS



Paul Lambert
Lead Portfolio Manager

19 / 24
YEARS ON FUND / YEARS AT WASATCH



Mike Valentine
Lead Portfolio Manager

6 / 7
YEARS ON FUND / YEARS AT WASATCH



JB Taylor
Portfolio Manager

23 / 27
YEARS ON FUND / YEARS AT WASATCH

*The performance data quoted represents past performance. Past performance does not guarantee future results. Current performance may be lower or higher than the data quoted. For the most recent month-end performance data, visit wasatchglobal.com. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. The Advisor may absorb certain expenses, without which total returns would have been lower. Wasatch Funds will deduct a 2% redemption fee on Fund shares held 60 days or less. The performance data does not reflect this redemption fee or taxes. **Total Expense Ratio: Investor Class—1.17% / Institutional Class—1.06%. The Advisor has contractually agreed to limit certain expenses to 1.50% for the Investor Class and 1.05% for the Institutional Class through at least 1/31/2025.***



top five stocks out of hundreds in the Index would have caused it to lose about two-thirds of its return for the quarter.

Generally speaking, we think stocks rose or fell during the first quarter based on four main factors:

1. The aforementioned *speculative* activity—rather than *investment* activity—surrounding AI and technology in general
2. The back-and-forth economic debate over recession, soft landing or continued expansion
3. The resulting outlook for inflation and interest rates
4. The reporting of revenues and earnings by individual companies

At Wasatch, we spend very little time and effort on the first three factors. As for the fourth factor, that's a top priority for us. But our investment horizon is measured in years, not quarters. So we typically keep our heads down, tune out most of the macro noise and focus on company fundamentals. We believe that if we consistently capture double-digit revenue and earnings growth—and if we pay rational prices for stocks—investment performance will take care of itself over the *long term*.

Although the *short term* isn't our main concern, there's been an interesting development in this respect. Positive and negative reports regarding revenues and earnings have been having larger and quicker impacts on stock prices. A separate short-term development is that we're generally not seeing as much potential for expansion in price/earnings multiples. These two developments have our senses heightened because there's less margin for error in calculating earnings-growth estimates, which are important components of the models we use to project future investment returns.

DETAILS OF THE QUARTER

The top contributor to Fund performance during the first quarter was **HealthEquity, Inc. (HQY)**, the largest U.S. non-bank custodian for health savings accounts (HSAs). Along with its primary business of offering HSAs, the company facilitates employer-sponsored lifestyle and commuter benefits. The stock was down late last year because investors were expecting an environment of lower interest rates that would cause the company to earn less income from money held on deposit for customers. Our analysis gives us visibility into HealthEquity's long-term earnings-growth potential, which we believe will remain strong for years to come. This insight gave us confidence to add to our position when the stock price dropped. During the first quarter, the stock climbed based on strong revenue and earnings growth—and we think the company's annual growth rates will stay in the double digits for the next several years.

Saia, Inc. (SAIA) was also a meaningful contributor. This freight company creates efficiencies by combining shipments (from multiple customers) that alone would fill "less than a full truckload" ("LTL"). Additionally, Saia's specialized logistics capabilities are important competitive advantages. Over periods of several years or more, we're confident in the company's ability to generate double-digit annual revenue and earnings growth. But the freight business is often cyclical, which can make investment returns "lumpy." For example, Saia's most recently reported revenues and earnings were especially strong—sending the stock price dramatically higher during the first quarter. In volatile names like Saia, we often trim our positions on strength and add more shares on weakness.

Another substantial contributor was **Medpace Holdings, Inc. (MEDP)**. The company is a contract research organization (CRO) supplying clinical development services to small biotechnology businesses. Medpace continues to post strong revenue and earnings growth as it provides critical services for its customers. The stock also benefited in the quarter from optimism that lower rates will help biotech companies more easily secure much-



needed funding for future clinical development. Although Medpace isn't a traditional biotech company, we believe it gives us some exposure to the industry without the typically poor cash flows of biotech businesses. Moreover, Medpace has continued to defy the skeptics by generally maintaining strong growth (often in double digits) and healthy fundamentals for years on end—even during several periods when biotech businesses have struggled.

The greatest detractor from Fund performance during the first quarter was **MarketAxess Holdings, Inc. (MKTX)**, which offers an electronic trading platform that we believe is pivotal for delivering efficiency, liquidity and cost savings to clients operating in global fixed-income markets. After a strong finish in 2023, the stock declined at the beginning of this year due to some concerns about potential market-share losses. Nevertheless, our investment thesis remains on track. We believe MarketAxess has been fine-tuning its services to accommodate clients of various sizes. And we don't think the recent competitive challenges will materially impact the company's ability to grow its global fixed-income trading business over the long term. We're especially excited about the revenue potential of some new services that help clients optimize operations and data flow. That said, MarketAxess is a volatile stock—and we strive to keep our position size at an appropriate level for risk management. During the first quarter, we took advantage of the stock-price weakness to buy more shares.

Clearwater Analytics Holdings, Inc. (CWAN) was also a major detractor. The company develops cloud-native software that allows clients to simplify their investment-accounting operations. Although management projected robust revenue growth of about 18% for the 2024 calendar year, analysts had been hoping for even better growth. As a result, the stock sold off. In our experience, Clearwater's management team tends to underpromise and then overdeliver. As a result, we bought more shares on the stock-price weakness. And we still expect annual revenue growth to exceed 20% for the next several years.

Another significant detractor was **YETI Holdings, Inc. (YETI)**, which designs, markets and distributes drinkware, coolers, and other outdoor and recreational gear. Although YETI's drinkware segment has performed reasonably well and its rollout of YETI-branded stores has shown promise, strong competitive threats have recently emerged in the drinkware space. So while YETI's stock price is attractive, we're maintaining a small position as we weigh whether the company can offset its slowing U.S. growth by successfully expanding internationally. *(Current and future holdings are subject to risk and change.)*

PORTFOLIO TRANSACTIONS

In the Core Growth Fund, we have a large weight in financials where we've been seeking to increase diversification by adding more positions. Among our buys during the first quarter, we added **Pinnacle Financial Partners, Inc. (PNFP)**, a bank based in Nashville, Tennessee with branches across the Southeast. We like Pinnacle because it follows a responsible banking model with a diversified customer base, a small securities portfolio, and appropriate levels of loans and deposits. Moreover, we believe Pinnacle is well-managed and serves a geographical area with a healthy real-estate market, favorable demographics and above-average economic growth.

Among our sells, we exited **Monolithic Power Systems, Inc. (MPWR)**, which designs and manufactures power-management solutions including power-conversion devices, LED lighting, load switches and other electrical components. With Monolithic's market cap now above \$30 billion, we redeployed those assets into smaller companies.



OUTLOOK AND POSITIONING

As described above, AI and technology more broadly drove much of the market returns during the first quarter. For example, within the Russell 2000 Growth Index, the top-performing companies during the period were MicroStrategy (MSTR) and Super Micro Computer (SMCI), whose stock prices more than doubled and more than tripled, respectively. We didn't own either of these companies, which aren't even small-caps. And we certainly didn't chase the quarter's top stock-market gainers.

Instead, we took note of *all* our companies' revenue and earnings reports. We then embarked on reanalyzing our companies and projecting their future growth rates. For the most part, our companies issued strong reports for the fourth quarter of 2023. And the growth rates we've projected for the 2024 calendar year are generally in double digits. Considering these projections and the reasonable valuations we're finding among small-caps—on an absolute basis *and* relative to large-caps—we're optimistic regarding investment performance going forward.

With respect to AI, we have no doubt that it will create massive positive changes in economies around the world. And these changes are likely to be even more significant than those created by the internet. But the internet revolution and other technological transformations have led to a myriad of very bad investments (the good ones notwithstanding).

In managing the Wasatch Core Growth Fund, we have three main considerations regarding AI:

1. We want to avoid companies whose business models will be materially *disrupted* by AI.
2. We're attracted to companies that will be able to *use* AI to strengthen their competitive positions and/or reduce costs.
3. Where possible, we're interested in *certain* companies directly involved in AI—but we're cognizant of the potential asymmetric risks and unreasonable valuations.

For more information on the current environment and our investment approach, please refer to the April 5th *Wasatch Market Scout* in the News & Insights section at wasatchglobal.com.

Thank you for the opportunity to manage your assets.

Sincerely,

Paul Lambert, Mike Valentine and JB Taylor



TOTAL RETURNS

FOR PERIODS ENDED MARCH 31, 2024

	Quarter*	1 Year	3 Years	5 Years	10 Years
Core Growth Fund—Investor	4.46%	28.00%	3.38%	12.97%	12.11%
Core Growth Fund—Institutional	4.48%	28.14%	3.51%	13.12%	12.24%
Russell 2000® Growth Index**	7.58%	20.35%	-2.68%	7.38%	7.89%
Russell 2000® Index*	5.18%	19.71%	-0.10%	8.10%	7.58%

*Returns less than one year are not annualized.

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Total Annual Fund Operating Expenses include operating expenses, including the management fee, before any expense reimbursements by the Advisor. **The Advisor has contractually agreed to limit certain expenses to 1.50% for the Investor Class and 1.05% for the Institutional Class through at least 1/31/2025.** See the prospectus for additional information regarding Fund expenses.

Wasatch Funds will deduct a 2.00% redemption fee on Fund shares held 60 days or less. The performance data does not reflect the deduction of fees or taxes, which if reflected, would reduce the performance quoted. For more complete information including charges, risks and expenses, read the prospectus carefully.

Investing in small cap funds will be more volatile and loss of principal could be greater than investing in large cap or more diversified funds. Investing in foreign securities, especially in emerging markets, entails special risks, such as currency fluctuations and political uncertainties, which are described in more detail in the prospectus.

An investor should consider investment objectives, risks, charges and expenses carefully before investing. To obtain a prospectus, containing this and other information, visit wasatchglobal.com or call 800.551.1700. Please read the prospectus carefully before investing.

Information in this document regarding market or economic trends, or the factors influencing historical or future performance, reflects the opinions of management as of the date of this document. These statements should not be relied upon for any other purpose.

The Wasatch Core Growth Fund's primary investment objective is long-term growth of capital. Income is a secondary objective, but only when consistent with long-term growth of capital.



** The Russell 2000 Growth Index measures the performance of Russell 2000 Index companies with higher price-to-book ratios and higher forecasted growth values.

† The Russell 2000 Index is an unmanaged total return index of the smallest 2,000 companies in the Russell 3000 Index. The Russell 2000 is widely used in the industry to measure the performance of small company stocks.

Indexes are unmanaged. Investors cannot invest directly in these or any indexes.

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Earnings growth is a measure of growth in a company's net income over a specific period, often one year.

Diversification is a strategy that mixes a variety of investments within a portfolio in an attempt to reduce risk. Diversification does not eliminate the risk of experiencing investment losses.

The price/earnings (P/E) ratio, also known as the P/E multiple, is the price of a stock divided by its earnings per share.

Revenue growth is the increase in a company's revenues over a specified period of time, not necessarily one year.

Valuation is the process of determining the current worth of an asset or company.

As of March 31, 2024, the Wasatch Core Growth Fund was not invested in MicroStrategy, Super Micro Computer or any of the "Magnificent Seven" companies (Alphabet, Amazon, Apple, Meta Platforms, Microsoft, Nvidia and Tesla).

CORE GROWTH FUND – TOP 10 HOLDINGS

AS OF DECEMBER 31, 2023

Security Name	Percent of Net Assets
RBC Bearings, Inc.	3.7%
Trex Co., Inc.	3.4%
Ensign Group, Inc.	3.1%
Guidewire Software, Inc.	3.0%
Hamilton Lane, Inc., Class A	3.0%
Balchem Corp.	2.8%
HealthEquity, Inc.	2.8%
Kadant, Inc.	2.7%
Globant SA	2.7%
ICON PLC	2.7%
Total	29.9%

Portfolio holdings are subject to change at any time. References to specific securities should not be construed as recommendations by the Fund or its Advisor. Current and future holdings are subject to risk.