

Kennedy Capital Management, Inc.

Micro Cap Commentary 3rd Quarter 2022

Market Review

The Russell Microcap[®] Index declined 0.48% in the third quarter of 2022, as US Federal Reserve rate increases and concerns regarding an impending recession remained top-of-mind for many investors. The distribution of returns by sector was significant in the quarter (a 26-percentage point spread between the best and worst), with six sectors declining by at least 7%, and only Health Care and Energy delivering positive returns. Performance in the Biotechnology industry was particularly robust (+16.6%), as acquisition activity and renewed optimism regarding drugs in development drove share prices higher.

Performance Recap

The KCM Microcap Composite returned -2.26% (gross of fees) and -2.44% (net of fees) in Q3, underperforming the Russell Microcap[®] Index by 178 basis points (gross) and 196 (net). While stock selection was modestly favorable in the quarter, sector allocation – particularly the underweight position in Health Care – resulted in the underperformance overall. On a year-to-date basis the portfolio has outperformed the benchmark by 542 bps gross of fees and 499 bps net. Additional performance information is included in the table below.

	1 Year	3 Years	5 Years	10 Years	Since Inception
Gross	-12.35%	10.60%	6.99%	12.47%	14.63%
Net	-12.97%	9.64%	6.02%	11.41%	13.56%
Index	-27.46%	6.86%	3.11%	8.37%	6.17%

Data as of 9/30/2022

The best performing sector in the Microcap portfolio this quarter was Industrials, adding 151 bps of outperformance during the quarter (182 bps from stock selection). The portfolio lagged in Health Care (180 bps unfavorable) and Consumer Discretionary (119 bps unfavorable). It's important to recognize that while our stock selection in Biotechnology was a positive contributor in the quarter, our underweight position in this industry was the primary driver behind the headwind from Health Care.

Outlook

We are entering the upcoming earnings season with a slightly larger cash balance vs. our typical level, reflecting patience in offsetting recent sales with new buys. We believe valuations of microcap

equities have become increasingly attractive, though in many cases earnings estimates for 2023 are too high given headwinds from interest rates, currency movements, and broader economic uncertainty. We anticipate deploying cash in the coming months as expectations adjust and clarity on the outlook for 2023 comes into focus.

Thank you for your support, and please don't hesitate to reach out with any questions or concerns.

Sincerely,

Christian J. McDonald, CFA®
Portfolio Manager

Sean McMahon
Portfolio Manager

Important Disclosures

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The Micro Cap Composite contains fully discretionary micro cap accounts that are invested primarily in micro cap companies (market cap generally in line with Russell Microcap® index market caps) which have strong intrinsic value. For comparison purposes the composite is measured against the Russell Microcap® Index. The U.S. Dollar is the currency used to express performance.

Composite specific data provided within this presentation has been calculated from accounts that are discretionary as defined in this paragraph. The assets shown are derived only from discretionary accounts. Non-discretionary accounts, as defined by KCM, are accounts that are not included in the composite due to one or any combination of the following criteria: there were significant cash inflows or outflows within the account; the account's asset level did not meet the minimum requirement to remain in the composite; the account assets are managed by others using our non-discretionary model. The temporary removal of such an account occurs at the beginning of the month and the account re-enters the composite the month after the criteria has been met.

Returns are presented gross and net of investment advisory fees and include the reinvestment of all income. Gross of fee returns reflects the deduction of transaction costs and custodian fees but do not reflect the deduction of investment advisory fees. Net of fee performance is calculated using gross returns less the actual applicable annual management fee applied monthly. A client's return will be reduced by the advisory fees as described in Form ADV Part 2A and other expenses incurred by the account. **Past performance is not indicative of future results.** For example, an annual advisory fee of 1% compounded quarterly over 10 years will reduce a gross 14.44% annual return to a net 13.32% annual return. Form ADV Part 2A is available upon request.

The performance figures reported herein are unaudited, may be based upon information obtained via electronic data sources ("feeds") and may be subject to change. Data feeds from many of KCM clients' selected custodians are obtained through third party, sources and are used to compare custodial data to KCM's client account records as frequently as daily. Monthly, KCM reviews clients' account holdings along with cash and share quantities against the custodial statements. In some instances, variances may exist between final audited custodial information and the information KCM obtains via such data feeds. Generally, any such variances are researched and reconciled within thirty days of the period end.

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Portfolio Sector Weightings are subject to change at any time. Sectors are based on the Global Industry Classification Standard (“GICS”) classification scheme and are measured as a percentage of the total composite in terms of asset value as of the date indicated above. Individual client portfolios may be different based on variations in security purchase price and date, and individual client restrictions. Due to rounding, Sector Weighting’s total percentages may not equal 100%.

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The Russell Microcap® Index measures the performance of the microcap segment of the U.S. equity universe. Microcap stocks make up less than 2% of the U.S. equity market (by market cap, as of the most recent reconstitution) and consist of the smallest 1,000 securities in the small-cap Russell 2000® Index, plus the next 1,000 smallest eligible securities by market cap. The Russell Microcap® Index is constructed to provide a comprehensive and unbiased barometer for the microcap segment trading on national exchanges, while excluding lesser-regulated OTC bulletin board securities and pink-sheet stocks due to their failure to meet national exchange listing requirements. The Index is completely reconstituted annually to ensure new and growing equities are reflected and companies continue to reflect appropriate capitalization and value characteristics.

The Russell Microcap® Index is used as the benchmark. The Index is unmanaged and represents total returns including reinvestment of dividends. The benchmark is used for comparative purposes only and generally reflects the comparable risk or investment style of the Firm’s strategy. The investment portfolios underlying the Index are different from the investments in the portfolios managed by the Firm. Certain accounts may also use other benchmarks not listed in the GIPS composite report. The Verification and Performance Examination Report does not cover the benchmark returns included in the GIPS composite report.

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