Kennedy Capital Management LLC

Mid Cap Value Commentary
3rd Quarter 2023

All major U.S. equity market indices posted negative returns during the 3rd quarter of 2023. The spread between large cap and small cap returns remains historically wide. Year-to-date, the Russell 1000 Index (large) is up +13.0%, compared to the Russell 2000 (small) up +2.5%.

The Kennedy Mid Cap Value (MCV) composite declined -4.19% (net of fees) during the quarter, outperforming the Russell MidCap® Value (RMV) by 0.27%. For the rolling 12-month period, the MCV composite returned 17.41% (net of fees), compared to the RMV's return of 11.05% outperforming by 6.36%. Additional performance information is included in the table below.

	1 Year	3 Years	5 Years	10 Years	Since Inception
Gross	18.18%	14.85%	8.14%	9.88%	11.44%
Net	17.41%	14.06%	7.39%	9.12%	10.65%
Index	11.05%	10.98%	5.18%	7.92%	9.01%

Data as of 9/30/2023

Within the RMV, Energy and Financials were the only two sectors to generate positive absolute returns in the quarter, returning 12.5%, and 1.0%, respectively. Communication Services, Health Care, and Consumer Staples were the three worst-performing sectors within the RMV, returning -10.1%, -9.9%, and -8.8%, respectively. Within the MCV composite, the Financials and Health Care sectors were the biggest contributor to positive relative returns (vs the RMV), adding 38 and 29 basis points, respectively, to 3rd quarter relative performance. On the downside, Industrials and Consumer Discretionary were the two biggest detractors from relative performance, negatively impacting 3rd quarter relative returns by 78 and 36 basis points, respectively.

Rising interest rates were the prevailing theme during the 3rd quarter. The yield on the 10-year treasury rate increased sharply over the three-month period, rising +76 bps to 4.57%, reaching the highest level seen since 2007. As discussed in previous commentaries, rising rates have several (negative) implications for financial markets:

1) **Higher discount rates, which equates to lower values for a broad range of financial assets (equities, bonds, etc.).**

Example: Devaluation of financial assets has been felt most acutely in more speculative areas of the market, such as SPACs (Special Purpose Acquisition Vehicles). SPAC returns in aggregate are down more than 40% from their peak in 2022, according to the S&P SPAC Index.

2) **Tighter access to capital, which restricts capital investment and slows economic growth.**

Example: According to the senior loan officer surveys conducted by the Federal Reserve, the net percentage of domestic banks tightening standards for commercial and industrial loans to large/middle market firms is at the third highest level seen in the last 20 years (just shy of 2020-2021 during COVID, and the Great Financial Crisis in 2009).

3) Higher borrowing costs, which erodes corporate profitability.

Example: BAA corporate bond yields – which reflect borrowing costs for companies that carry "moderate" credit risk – have more than doubled off the 2020/2021 lows and are now at 10+ year highs.

Despite the tighter financial conditions, the US economy thus far appears to be holding up well. Unemployment rates are at multi-decade lows, Corporate earnings—while down versus the highs experienced in 2022 – are still tracking well ahead of pre-COVID levels, and credit spreads (a barometer of economic + corporate stress) remain at benign levels. Inflationary pressures are still present, but the rate of change continues to slow from the peak in mid-2022. We remain watchful of how the tightening financial market conditions are impacting the economy, and underlying business fundamentals.

Experience tells us the most attractive long-term investment opportunities present themselves during times of heightened uncertainty and bearish market sentiment. When evaluating potential investments for the portfolio, regardless of the macroeconomic environment, we always fall back on first principles:

1. Does this business typically generate returns above its cost of capital over a market cycle, and are there opportunities to reinvest back into the business at attractive rates of return?
2. Based on our fundamental research, what impacts do we see to the business that could alter its returns trajectory and reinvestment opportunity set (for better, or for worse) over the next 3-4 years?
3. What is currently priced into the stock, and does it differ from our fundamental outlook for the business?

By staying disciplined to our process, we can construct a portfolio of companies that in aggregate have superior fundamental attributes relative to the overall market, but at valuation levels that give us an adequate margin of safety. We believe this is a winning recipe for compounding returns over the long term.

We welcome the opportunity to discuss any questions or concerns you may have, and we thank you for the opportunity you have given us to manage your account.

Sincerely,

Frank Latuda, Jr. CFA®
Chief Investment Officer & Portfolio Manager

Gary Kauppila, CFA®
Portfolio Manager

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The Mid Cap Value Composite invests in US equity securities and ADRs with market capitalizations that are reflective of the Russell Midcap® Value Index. The portfolio manager focuses on companies with a demonstrated ability to generate above-average returns on invested capital. Within that universe, the manager seeks to identify undervalued companies with opportunities to reinvest cash flows at rates of return in excess of their cost of capital. For comparison purposes the composite is measured against the Russell Midcap® Value 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.

Performance returns are presented gross and net of investment advisory fees and include the reinvestment of all income. Gross of fee returns reflect 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. ***Past performance is not indicative of future results.*** *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. 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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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.

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Allocations to various assets classes change over time and deviate from any stated or targeted percentages of a total portfolio as a result of market conditions and reallocation decisions. Therefore, nothing herein reflects a static portfolio allocation that will remain the same or match stated target allocations of asset classes.

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The Russell Midcap® Value Index measures the performance of the mid-cap value segment of the U.S. equity universe. It includes those Russell Midcap® Index companies with relatively lower price-to-book ratios, lower I/B/E/S forecast medium term (2 year) growth and lower sales per share historical growth (5 year). The Russell Midcap® Value Index is constructed to provide a comprehensive and unbiased barometer of the mid-cap value market. The Index is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true mid-cap value market.

The Russell 1000® Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000® Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000 represents approximately 92% of the U.S. market. The Russell 1000 Index is constructed to provide a comprehensive and unbiased barometer for the large-cap segment and is completely reconstituted annually to ensure new and growing equities are reflected.

The Russell 2000® Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000® Index is a subset of the Russell 3000® Index representing approximately 7% of the total market capitalization of that index, as of the most recent reconstitution. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. The Russell 2000® is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set.

The Russell Midcap® Value 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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