Kennedy Capital Management LLC

SMID Cap Growth Commentary
4th Quarter 2023

Equity markets returns in 2023 were ultimately quite constructive, but the path was very volatile and dominated by expectations for interest rates. All year long, market participants were hyper-focused on every nuanced bit of news that might indicate the future path of the Fed Funds Rate, a key macro factor that will impact the depth and duration of this business cycle. While the Federal Reserve steadily increased the Fed Funds Rate during the year, from 4.5% at the start, to the current 5.25 - 5.50% level, it is the longer term 2 & 10-year Treasury yields that imbed the market's expectations of the *future* Fed Fund path (and thus the economy as well). Simply looking at the 10-year Treasury yield's small increase between the year's beginning & ending levels (3.5% and 3.9%, respectively), one might have thought that 2023 bore few surprises. However, the path of this yield was much more volatile, peaking at 5% in October and then dropping dramatically in the last two months of the year, largely explaining the hyper-volatile moves in the equity markets. Commentary from the Fed Chair indicating that we have seen the end of rate hikes this cycle was the catalyst for the most recent Q4 rally.

Negative earnings revisions were the other primary driver of both individual company and overall market returns in 2023, as the impacts of normalizing inventory levels, slowing inflation, and weaker pockets of demand became fully realized. These impacts were more acutely felt by smaller-capitalization companies which comparatively skew more cyclical and/or are impacted by physical supply chains.

Overall, despite the volatility, the macro-economic backdrop ended up being roughly as we originally expected (i.e., settling around 4%ish long-term rates & a "soft landing" for the economy) and a reasonable environment for investing behind growth. The result was a very strong absolute and a reasonable relative performance for the strategy, during a year that was certainly trickier than usual to navigate.

Performance:

The KCM SMID Cap Growth (SMIDG) composite increased +15.09% (gross of fees) and +14.89% (net of fees) for the 4th quarter of 2023, outperforming the Russell 2500™ Growth (R25G) Index, which increased +12.59%, by +250 bps (gross of fees) and +230 bps (net of fees). Year-to-date the KCM SMIDG composite increased +19.85% (gross of fees) and +19.07% (net of fees), outperforming the R25G Index, which increased +18.93%, by +92 bps (gross of fees) and +14 bps (net of fees). Additional performance information is included in the table below.

	1 Year	3 Years	5 Years	10 Years	Since Inception
Gross	19.85%	-0.36%	13.54%	9.74%	12.79%
Net	19.07%	-0.98%	12.87%	9.00%	11.96%
Index	18.93%	-2.68%	11.43%	8.78%	11.40%

Data as of 12/31/2023

On a relative basis, Information Technology and Financials were the best-performing sectors versus the benchmark. The strength in Information Technology was led by a leader in the data integration market with software that connects, manages, and unifies data across any multi-cloud hybrid system. The stock responded to a solid Q3 result and subsequent investor day, where they laid out an expectation for multi-year accelerating ARR and total revenue growth, benefiting from past R&D investments and a shift of sales and marketing resources to their Cloud solutions. We expect this will also drive significant operating leverage. Within Financials, a top contributor was a banking and financial services holding company. The company benefited from the decline in interest rates during the period, but more importantly they also announced the opportunistic purchase of two portfolios of Commercial Real Estate loans from the FDIC at 63% of par value. While standalone, this is a financially attractive deal and likely accretive to earnings for an extended period of time, even more important to the stock is that this indicates that they are in a strong position to take advantage of recent market dislocations.

Our largest detractors to relative performance for the quarter were Industrials and Health Care. One of the material drags on the Industrials performance was a manufacturer of ground mounting systems used in utility-grade solar projects. It's sales disappointed as they saw several large project timelines get pushed out, and. their key competitor has not seen a similar impact- leading to concerns of structural market share loss. We continue to hold the shares as we believe these revenue differences are temporary, and the company has visibility into ramping project demand for 2024/2025. Within Health Care, the Biotechnology industry was the largest detractor. There was not one specific holding driving this result; rather, our entire basket of names contained no big positive trial result or acquisition take-out winners, unlike the Index. In addition, our structural underweight was a drag during a period of strong sector returns.

For the calendar year 2023, the strongest areas of relative performance came from Consumer Staples and Financials. Industrials and Information Technology were the largest detractors to performance.

Outlook:

Entering 2024 there is improved visibility on the key macro inputs, which should enable investors to return the focus to individual company earnings execution and longer-term growth opportunities. We believe the next meaningful leg of market performance will require improving corporate earnings, and this should also lead to a broadening out of the market, benefiting smaller-capitalization stocks. While incremental macro-economic data continues to support the consensus view that "peak rates" are in, we do anticipate some continued volatility relating to the exact timing and realization of future rate reductions vs. expectations. This makes any short-term relative performance difficult to predict, but we believe that our strategy of investing in companies with higher CFROIs (cash flow return on investment) and higher asset growth (i.e., re-investment opportunities) will mean that they are better positioned to deliver on earnings growth expectations over the next couple of years. Assuming our companies can execute against these growth opportunities, we believe this should be a recipe for longer-term outperformance.

Thank you for your continued confidence in the Kennedy Capital team. Should you have any additional questions, please do not hesitate to contact us.

Sincerely,

Jean Barnard, CFA®
Portfolio Manager

Ryan Dunnegan, CPA
Assistant Portfolio Manager

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The SMID Cap Growth Composite invests in growth securities of predominately small and mid cap companies that generally have a market capitalization that is reflective of the Russell 2500™ Growth Index. The Manager seeks companies with durable *business models able to deploy assets into growing sets of opportunities providing superior rates of return. For comparison purposes the composite is measured against the Russell 2500™ Growth 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.*

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The Russell 2500™ Growth Index measures the performance of the small to mid-cap growth segment of the U.S. equity universe. It includes those Russell 2500™ companies with relatively higher price-to-book ratios, higher I/B/E/S forecast medium term (2 year) growth and higher sales per share historical growth (5 year) The Russell 2500™ Growth Index is constructed to provide a comprehensive and unbiased barometer of the small to mid-cap growth market. The Index is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small to mid-cap opportunity set and that the represented companies continue to reflect growth characteristics.

The Russell 2500™ Growth 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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