Kennedy Capital Management LLC

Small Cap Growth Commentary
4th Quarter 2022

While Q4 provided a welcome reprieve and possibly the first indication that we can begin to look forward to a market backdrop that is more constructive for individual stock-selection, as a whole 2022 was a disappointing year for investors, particularly those investing in growth-oriented strategies. Excessive inflation was the main culprit – a result of COVID stimulus, easy money, supply constraints, and geopolitical conflicts. In response to this, the Federal Reserve implemented a series of sharp interest rates increases, which directly caused a reset of equity discount rates (lessening the value of future cash flows) and is expected to have a negative drag on demand (and thus estimates for near-term earnings potential). The result was declining equity markets and underperformance, even within the Russell 2000® Growth Index, of companies with "growthier" characteristics (i.e., higher sales & earnings growth rates and higher valuations).

Performance:

The KCM Small Cap Growth (SCG) composite increased +7.29% (gross of fees) and +7.08%% (net of fees) for the 4th quarter of 2022, outperforming the Russell 2000® Growth (R2G) Index, which increased +4.13%, by +316 bps (gross of fees) and +295 bps (net of fees). For the calendar year 2022, the SCG composite decreased -26.06% (gross of fees) and -26.63% (net of fees) vs. the R2G Index, which decreased -26.36%, outperforming by +30 bps (gross of fees) and underperforming -27 bps (net of fees). Additional performance information is included in the table below.

	1 Year	3 Years	5 Years	10 Years	Since Inception
Gross	-26.06%	5.04%	8.58%	12.89%	13.92%
Net	-26.63%	4.27%	7.83%	12.09%	13.10%
Index	-26.36%	0.65%	3.51%	9.20%	9.72%

Data as of 12/31/2022

On a relative basis, Consumer Staples and Consumer Discretionary were the best-performing sectors versus the benchmark. The strength in Consumer Staples was again led by a provider of branded, affordable cosmetic and skin-care products. The company has continued to demonstrate strong sales momentum primarily due to the launch of new products and brands. The company has also been successful in increasing prices, which should aid margins in the future, particularly as supply-chain cost pressures ease. The top individual contributor to Consumer Discretionary was an owner and operator of hotels & casinos in Colorado and Nevada. The stock was up meaningfully following the announcement of their Q3 results as they continued to out-execute, with strong revenue growth and profit conversion, following the completion of a major renovation and expansion of their properties.

Our largest detractors to relative performance for the quarter were Energy and Materials. This was due to our lack of ownership in either sector during a period they both outperformed and following their increased weightings in the benchmark. Our investment strategy does not invest in commodities or companies whose returns are highly dependent solely on those price movements. As a result, we currently have a large underweight in both sectors which likely will result in more volatile short-term results vs. the Index.

For the calendar year 2022, relative performance was positive in the top outperforming sectors of Consumer Staples and Consumer Discretionary. Health Care and Energy were the largest detractors to performance.

Outlook:

While the macro backdrop remains volatile, valuations and earnings expectations have declined significantly from their peaks in 2021, increasingly presenting us with more attractive long-term opportunities to consider. As a result, we have started the process of slowly deploying our excess cash into new and existing investments where we have conviction in the medium-term earnings potential vs. market expectations. That said, we believe there is still significant risk as to exactly where things land in 2023/2024 – both to the upside and the downside – and expect that near-term the equity markets will continue to be dominated by any news on the same key macro factors: inflation, interest rates, and demand destruction. For this reason, we are taking a deliberately slow and methodical approach to any changes in the portfolio holdings. But we still believe that at some point in 2023, visibility on these key macro inputs should settle out and investors will again focus on individual company earnings execution and longer-term opportunities. We spend the majority of our time preparing the portfolio for that day, understanding how the new environment impacts our companies' returns but making sure to keep our focus on the 3–to-5-year growth opportunities. In aggregate, the portfolio is invested in companies with higher CFROIs (cash flow return on investment) and higher asset growth (i.e., re-investment opportunities), trading at a roughly similar valuation as the benchmark (based on current & next year P/Es). 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
Portfolio Manager

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The Small Cap Growth Composite invests in growth securities of predominately small companies that generally have a market capitalization that is reflective of the Russell 2000® 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 2000® 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.*

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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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 2000® Growth Index measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000® 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 2000® Growth Index is constructed to provide comprehensive and unbiased barometer for the small-cap growth segment. The Index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect growth characteristics.

The Russell 2000® 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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