Kennedy Capital Management, Inc.

Small Cap Select Commentary
3rd Quarter 2022

The Market:

US equity markets experienced a volatile third quarter. Small cap stocks were up over 18% in early August only to end the quarter down more than 2%. The volatility was driven by investors' hope that inflation had peaked, followed by the realization that prices continue to climb. Core inflation, a measure of prices that strip out volatile spending categories such as energy and food, again exceeded expectations and even accelerated in some areas of the economy. In response, the US Federal Reserve continued their rate hiking strategy. The Fed's commentary since then has become more forceful that rates will move higher still and, more importantly, remain there well into the future.

The majority of the market's downtrend this year is the result of pricing in higher discount rates for longer. Eventually, the Fed's policies will impact demand in the real economy beyond the already hit homebuilding industry. As a result, we anticipate earnings and corporate results will be an even greater differentiator over the coming quarters. The impact on sectors, industries, and individual companies will vary and we are taking the economic environment into account. There continues to be various paths that inflation, the Fed, or the war in Ukraine could take that significantly changes the macro trajectory. We will remain balanced and data dependent as we invest in companies that are able to execute on their own value enhancing catalysts.

Performance:

For the third quarter of 2022, the Select Composite experienced a return of -5.95% (gross of fees) and -6.15% (net of fees) as compared to the Russell 2000®, which returned -2.19%. Year-to-date, the Select Composite experienced a return of -26.66% (gross of fees) and -27.14% (net of fees) as compared to the Russell 2000®, which returned -25.10%. Certain account performance may vary from this composite performance due to client-initiated account restrictions on certain types of holdings or due to client cash flows. Additional performance information is included in the table below.

	1 Year	3 Years	5 Years	10 Years	Since Inception
Gross	-21.65%	6.46%	4.68%	8.49%	11.54%
Net	-22.33%	5.53%	3.76%	7.53%	10.12%
Index	-23.50%	4.29%	3.55%	8.55%	8.51%

Data as of 9/30/2022

The Health Care sector was our largest area of relative underperformance in the quarter. The biotechnology group in the benchmark performed well, but we are underweight, and our individual investments lagged the market's returns. While we did invest in two new biotech stocks during the third quarter, this did not increase our weighting as they replaced our investment in another biotech stock, which was acquired. A digital IT consulting firm was our worst performing stock. The company experienced project pauses and cancellations, and the stock was sold off on fears of lower growth. While there is the potential for choppy results in the near term, we believe these results are not related to competition or structural changes in the industry. We continue to hold the stock and believe the company can gain share and expand margins over time due to their unique mix of global assets and competitive pricing.

The Consumer Staples sector was our best relative performing group and was driven by our best individual stock, which sells cosmetics and skin care products through retailers and their own e-commerce store. The company continues to take market share, expand their product line-up, increase brand awareness, and improve their business operations. Over the past several quarters, they've seen meaningful growth in product volumes and average selling prices which has driven strong earnings results. We remain invested here but trimmed the position as it approached a 4% weighting to manage risk.

<u>Portfolio Positioning, New Investments, and Positions Exited</u>:

As of September 30th, we are overweight the Industrials, Consumer Staples, and Health Care sectors. We are underweight the Materials, Communication Services, and Utilities sectors. The portfolio also remains underweight cyclical industries as compared to the benchmark.

<u>The Future</u>:

We anticipate the coming months will continue to be volatile. Uncertainty surrounding the duration of the Fed's inflation fight and a potential economic slowdown remain high. As we wrote earlier, the path that events could take is multi-pronged and our goal is to remain balanced. Even with the outstanding worries, we believe the longer-term setup for small cap stocks is intriguing. Several absolute and relative valuations for the Russell 2000® small cap index are near or below trough levels seen over previous decades. As such, we remain focused on investing in companies that can execute on their catalysts to create value.

Thank you for your continued confidence in us. Should you have any questions or concerns, never hesitate to call.

Sincerely,

Alex Mosman, CFA®
Portfolio Manager

Important Disclosures

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The Small Cap Select Composite contains fully discretionary small cap accounts that are invested in small cap value and small cap growth companies that demonstrate valuation below, return on assets above and return on equity above those of the Russell 2000® Index, while observing tax sensitivity strategies. For comparison purposes the composite is measured against the Russell 2000® 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 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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Portfolio Sector Weightings are subject to change at any time. Sector weightings are based on the Global Industry Classification Standard ("GICS") classification scheme and are measured as a percentage of the total portfolio 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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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 2000® 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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