SMALL CAP DISCOVERIES

Portfolio Comments
March 31, 2023

Distinguishing Features

GIM builds the Small Cap Discoveries portfolio from the bottom-up; sector weightings are secondary to stock selection. Since last quarter, the Small Cap Discoveries portfolio maintained a significant overweight in Health Care versus the Russell Microcap Growth benchmark. We are also overweight Consumer Discretionary and Technology. The portfolio is equal weight to the benchmark in Basic Materials and underweight in all other sectors. The portfolio has no exposure to Utilities, Real Estate, Consumer Staples, or Energy.

Market Environment

The turmoil in the banking sector brought a volatile end to the first quarter and a reappraisal of the Federal Reserve's policy priorities. Q1 served up highs and lows - shifting positively on declining inflation numbers in January, then declining on fears of an overheating economy in February and shifting again to contend with banking stress and credit crunch fears in March.

It is still too early to have a confident view on the implications of the current banking turmoil for the US economy. Our expectation, however, is that reduced credit availability will prove to be a headwind, which may help the Fed with its lower growth/ lower inflation goals, despite rising real income and better global growth. The risk of recession has risen, given the Fed's steep interest rate increases and their impact on banks and lending. Investors have moved money away from regional banks and into higher yielding money market funds. Lack of deposits forces banks to lend less, and what they do lend comes at higher rates.

Performance Discussion

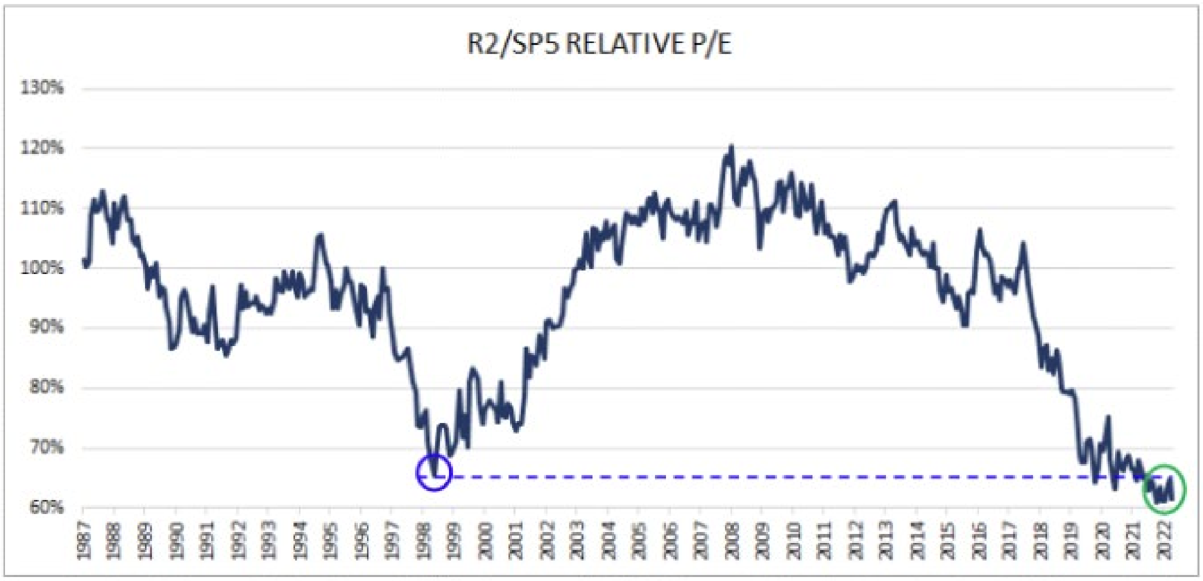
The Granahan Discoveries strategy returned +9.3%, nicely outperforming Russell Microcap Growth Index return of +0.8%, and the +6.1% of the secondary Russell 2000 Growth benchmark.

The strategy's best performing stocks for the quarter were **Harvard Biosciences** (Health Care, Special Situation), **Materion** (Basic Materials, Core Growth), **Green Brick Partners** (Consumer Discretionary, Core Growth), **SI-BONE** (Health Care, Pioneer), and **Beauty Health** (Consumer Discretionary, Core Growth). Biggest detractors were **Bluebird Bio** (Health Care, Pioneer), **Kezar Life Sciences** (Health Care, Pioneer), **Texas Capital Bancshares** (Financials, Special Situation), **Olink Holding** (Health Care, Pioneer), and **Kiniksa Pharmaceuticals** (Health Care, Pioneer).

In terms of our Lifecycles, Core Growth and Special Situations nicely outperformed the benchmark while Pioneers lagged this quarter.

Tighter credit conditions will likely remain a headwind to economic growth but could also alleviate the need for the Federal Reserve to slow economic growth through more interest rate increases. While the quarter's banking crisis brings up memories of the 2007-2008 global financial crisis, the fundamental nature of the challenge now is very different. The crisis today is focused on liquidity and duration of securities portfolios compared to credit losses during the GFC.

While we are cognizant about the weakening economic conditions given constrained credit and higher interest rates, we remain committed to our process for finding great long-term growth opportunities especially those early in their lifecycle with disruptive products addressing large markets. Today, small cap valuations sit at historic lows relative to large capitalization stocks.



Source: Furey Research Partners and FactSet. Data as of 3/31/23. Represents median P/E using latest available trailing 12-month earnings. Profitable companies only.

Earnings estimates have come down; however, the growth rates for the overall Discoveries portfolio are expected to outpace those of the general economy and of the comparable benchmarks. Despite the current volatility in the overall markets, we have a high conviction given our belief that the risk-reward tradeoffs for our holdings are more attractive than they have been in years.

Outlook

The Small Cap Discoveries portfolio leverages GIM's team of experienced portfolio managers who are also sector specialists. We remain committed to our process for finding great long-term growth opportunities by identifying companies early in their lifecycle with disruptive products addressing large markets. The value-creation process for these types of companies plays out over years, making patience and opportunistic position sizing key components of our investing process. While the portfolio's performance during the first quarter of 2023 was modestly below benchmark, we've seen several recent value creating events play out for our companies as we had expected. And importantly, the positive news flow correlated with strong stock upside, which was not always the case when the market was in momentum mode. This reinforces our conviction that the risk-reward tradeoffs for many of our holdings are more attractive than they've been in years, affording us the opportunity as we move through 2023 to continue tilting the portfolio modestly toward names with value-creating catalysts on the near- to medium-term horizon.

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