



## SMALL CAP CORE INVESTMENT COMMENTARY & REVIEW

by Quinn Stills

Fourth Quarter 2022

Our outlook for 2023 continues to be optimistic. Our outlook is perhaps a contrarian view, given the steep decline the markets have experienced, especially in August, September and, then again, in December as the fourth quarter of 2022 came to a close. We still believe that the catalyst for a strong rally will be inflation fears peaking and then receding, as we move into the middle of 2023. As we wrote previously, the Federal Reserve is in the process of re-setting interest rates to higher levels as a means to curb the rampant inflation that has gripped the economy, and it is working.

Why do we remain optimistic? Because some signs of inflation are coming down. For example, according to the Bureau of Labor Statistics, the Consumer Price Index fell -0.1% in December, which was the lowest reading since 2020. While the 12-month CPI fell slightly to 6.5%, it was nevertheless the lowest 12-month reading since October of 2021. Looking back at the last 7 months, the CPI is running at a rate of 2.2%. If we annualize the 4th quarter of 2022, the CPI is running at a subdued rate of 1.6%! Clearly, inflation is in decline and, moreover, the rate of decline accelerated in December.

The fourth quarter witnessed a stubbornly firm, hawkish tone from the Federal Reserve but a moderation of high inflation data in the mainstream economic statistics for the United States. The market rallied sharply in October, more moderately in November but then lost some of those gains in December. For the quarter, the Small Cap Core Strategy slightly underperforming the 6.23% increase in the benchmark Russell 2000 index. For the fourth quarter of 2022, the top performing

sectors in the portfolio included communications services, industrials, and utilities. Also, for the quarter, the weakest performing sectors included consumer discretion, health care, and financials.<sup>1</sup> Turning to the stock level of analysis, the top performing individual stocks included Willis Lease Finance, Sanara Medtech, Tecnoglass, and AEHR Test Systems. The weakest performing stocks included Rogers Corp, Enovix, Aeva, and Innoviz Tec, LTD.

The Small Cap Core Strategy is set up to thrive when interest rate changes begin to stabilize. The portfolio is, in some respects, like a crouching tiger or hidden dragon. PIA has an overweight in information technology, financials and industrials. The technology sector, in particular, is on sale. For perspective, virtually none of the portfolio's technology companies have any net debt. We believe the balance sheets of the portfolio's technology companies are fortified and might easily withstand a recession. Of note within technology, the portfolio recently initiated a significant investment in the electronic vehicle marketplace. The portfolio is invested in semiconductor stocks that are suppliers into the market for self-driving electric vehicles and advanced-driver-assisted vehicles and components. For perspective, we believe that the information technology sector is inexpensive and that current market conditions are providing the opportunity to buy these companies at an historic discount. Having been a professional investor since 1984, it is important to recall that there are very few times when fast growing, highly innovative companies in technology are selling at such steep discounts. We believe that this is one of those times.

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<sup>1</sup> *For informational purposes only, the specific investments shown represent only the top contributors and detractors for the relevant performance time period. The selection criteria used to determine the top contributors and detractors remains the same across performance measurement periods.*

*The Russell 2000 index measures the performance of the 2,000 smallest companies in the Russell 3000 index. The Frank Russell Company created the index in 1984, and it was one of the first broad benchmarks of the U.S. equity market.*

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