SMALL CAP DISCOVERIES

Portfolio Comments
September 30, 2024

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 has maintained its overweight in Health Care and Consumer Staples and has added to its overweight in Information Technology and Consumer Discretionary versus the Russell Microcap Growth benchmark. The portfolio is equal weight in Materials and underweight in all other sectors. The portfolio has no exposure to Utilities or Energy.

Market Environment

The most significant macroeconomic development during the quarter was the Federal Reserve's decision to cut interest rates by 50 basis points in September. While a reduction in rates is certainly welcome, macroeconomic and geopolitical concerns continue to weigh on investor sentiment, and small cap stock returns continue to lag behind those of large caps.

Part of the reason small caps have lagged since the Fed cut rates may have been doubts about the economy. Inflation looks to be headed in the right direction, and jobs growth suggests an economic 'soft landing.' The outlook is not without risk, however. Tensions in the Middle East are escalating, US elections are weeks away, and wage growth is up some, all concerns for the market. A strong jobs market and re- acceleration in wage growth could mean fewer rate cuts than expected, however, overall the macro picture remains positive.

Performance Discussion

In the third quarter, the Granahan Discoveries strategy returned +5.5%, underperforming the Russell Microcap Growth Index return of +8.6%, and the +8.4% return of the secondary Russell 2000 Growth benchmark.

With regards to LifeCycles this quarter, Pioneer outperformed while Special Situation and Core Growth underperformed the Index.

Top Contributors	Top Detractors
1. Edgewise Therapeutics (Health Care, Pioneer)	1. PROS Holdings (Tech., Core Growth)
2. Mayville Engineering (Industrials, Special Sit.)	2. Veeco Instruments (Tech., Special Sit.)
3. Zymeworks, Inc. (Health Care, Pioneer)	3. Vivid Seats (Communication Svs., Special Sit.)
4. CEVA, Inc. (Tech., Special Sit.)	4. PDF Solutons (Tech., Special Sit.)
5. Kiniksa Pharmaceuticals (Health Care, Pioneer)	5. OrthoPediatrics (Health Care, Core Growth)

Top Contributors in Q3:

- **Edgewise Therapeutics** is a leading muscle disease biotechnology company developing novel therapies for muscular dystrophies and serious cardiac conditions. During the quarter, the company provided first in human data for a development therapy targeting hypertrophic cardiomyopathy (HCM) which is the most common genetic heart condition resulting in thickening of the heart muscle. The results showed clear efficacy and no safety concerns. While the data are early, we have increased confidence in this opportunity that still represents meaningful upside to the stock.
- **Mayville Engineering** is the largest metal fabricator in the country providing tooling, coating, assembly, and aftermarket services to equipment OEMs in the construction, agriculture, powersports, and commercial vehicle markets. MEC's financial results have been robust especially relative to its end markets that have shown some softness. These results confirm our thesis of MEC's ability to gain market share as they provide an outsourcing solution for large OEMS. We believe interest rate cuts would turn into a tailwind for the business next year as lower financing costs would lead to an uptick in vehicle purchases.
- **Zymeworks** is a biopharmaceutical company with expertise in protein engineering leading to a differentiated pipeline of ADCs and multispecific antibodies targeting numerous cancers and has recently expanded into autoimmune and inflammatory disease. The stock performed well during the quarter as its proprietary pipeline advanced and a key partnered program moved closer to FDA approval.
- **CEVA** architects, develops, and licenses comprehensive communications and scalable edge AI IP that delivers high performance at ultra-low power enabling consumers to deliver quality products. CEVA powers many smart edge products and powers more than 18 billion products. The company reported very strong financial results and demonstrated traction with AI design wins that position the company well over the next several years.
- **Kiniksa** is a biopharmaceutical company focused on discovering, developing, and commercializing medicines designed to modulate immunological signaling pathways for patients suffering from debilitating diseases. Arcalyst, a therapy to treat recurrent pericarditis, continues to exceed expectations. Additionally, we expect updates on a therapy targeted at autoimmune disease to be positive and give investors increased confidence in the development of a second commercial product.

Top Detractors in Q3:

- **PROS Holdings** provides a software platform that provides businesses with predictive AI insights in the form of product suggestions, personalized offerings, and real-time pricing across sales channels. The products have a demonstrated ROI in the form of revenue uplift and margin improvement. The stock was weak in the quarter given the company's exposure to the airline industry. Some of the carriers' operational challenges have led to softer bookings that will moderate growth over the next year.

- **Veeco** is a diversified supplier of semiconductor process equipment. The company's products help customers lower power consumption and manufacturing costs. AI is one driver of the company's business, and we saw weakness in AI infrastructure stocks during the quarter
- **Vivid Seats** operates an online ticket marketplace for major events in North America. While demand for live events is relatively resilient, there is some moderation from consumers given the past two years of post-pandemic concerts that were very strong. The concert lineup improves in 2025, so we expect the impact to be short-lived.
- **PDF Solutions** is a leading provider of yield improvement technologies for the integrated circuit manufacturing process. The company's technical software is used by foundries and fabless chip companies to drive higher yields. Given the pressure on AI infrastructure stocks and weakness at customer Intel, the stock was weak on a relative basis.
- **OrthoPediatrics** is a medical device company that develops and markets anatomically appropriate implants and devices for the treatment of children with orthopedic conditions. Over the last several years, the company has down an excellent job in building out its portfolio of products through organic investment and attractive M&A. KIDS can now meet most of a children's hospital's surgery needs that we believe will lead to meaningful market share gains over the next several years. The recent multiple compression has been tied to higher interest rates and investors skepticism towards healthcare companies investing in future growth initiatives. As KIDS meets its financial expectations, we expect the company to be recognized by investors given its market leadership position and attractive financial profile of growth and profitability.

Outlook

Earnings growth in our small companies has been hampered by slowing top line growth comparisons versus the pandemic era hyper-growth, as well as interest rate hikes that hindered customers' ability to spend.

> *"Small cap three-year returns turned meaningfully negative, something that has happened only four times since 1978. Such periods of stagnation are followed by strong recoveries. One thing we know about the market is that it moves in cycles. Large caps have been leading for over 13 years now, which is relatively long compared to history. Small-cap trailing 10-year relative return versus large-cap is near an 80-year low. These lows have been reached multiple times in the past and each time it looked as if small caps had been left for dead, only for them to recover strongly in the forward years. The question is when will the recovery begin."* -Furey Research, October 7, 2024.

Sales growth is beginning to recover with the outlook for 2025 strong for both revenue and earnings growth. We believe the companies in the portfolio are operating well with their secular demand drivers, pricing power and low financial leverage.