Denali Network Value Small
4Q 2021 Commentary

- The delta variant wave of Covid-19 subsided and gave way to omicron, more infectious but less severe. Rapid economic growth resumed in Q4, but inflation continued to rise, raising expectations of imminent monetary tightening and higher rates. Strong earnings pushed US equities ahead. The very largest Growth stocks retained their hold on investors and spurted higher, but Value and defensive sectors prevailed among mid and small cap stocks.
- Our **Network Value Small** composite gained 8.30% in Q4 gross of fees (8.20% net), while the Russell 2000 Value gained 4.36%, a 3.94% gross excess. The strategy returned 34.70% gross of fees (34.15% net) year-to-date, vs. 28.27% for the benchmark.
- Investors rewarded fundamental performance. Benchmark stocks with positive earnings for the past year gained on average over 8% for the quarter, while the nearly 40% of constituents reporting losses fell more than 4%.Our position favoring stocks with higher E/P ratios and avoiding loss makers accounted for about 320 bp of our active gain.
- Our Network Value Index*, focused on stocks with both higher earnings and lower liquidity, also gained 8.30% for Q4, basically accounting for our outperformance. The NV Index outperformed the benchmark by 7.21% for the year.
- Reflecting this performance, the stock-level Network Value forecast was again quite successful in Q4. Our Detailed Estimates forecast also had very good predictive performance. Characteristics Trend model results were barely positive amid continuing factor return volatility. Intrinsic Value model results were modestly positive.
- Linear attribution shows exposure to both higher forecast and reported E/P made large positive contributions in Q4, but the strongest by far was from higher Sales/Price. Cash Flow/Price was also beneficial, but B/P was slightly negative net of other factors. Lower volatility and higher ROE were highly beneficial, and higher sales/assets ratio returned to positive form. Lower beta and momentum moderately detracted. For the year, forecast E/P and S/P contributed most, but reported E/P was negative due to a dire first half. Lower beta was the most negative systematic impact for 2021.
- GICS sector allocation produced about a fourth of our active return; underweights to Health Care and Energy were most beneficial, while those to Utilities and Real Estate detracted. Selection within sectors was most successful in Financials (lenders), Industrials (building products), Real Estate (services), Staples (groceries) and Communications (no AMC). Only Discretionary had meaningful negative selection.

Market Outlook

Developments in the Covid-19 pandemic came as fast as ever, with Q4 beginning on the downslope of the delta variant wave of infections and ending with the explosion of omicron infections pushing case rates to the highest yet seen. Delta and cascading supply chain constraints significantly dented economic activity in the U.S. and abroad. U.S. GDP growth in Q3 came in at 2.3% over Q2, much lower than expected. However, the less severe illnesses caused by omicron have helped engender optimism for normalization, and quarterly growth in Q4 is estimated at 6%. Unemployment fell again to 4.2%, but labor force participation rates remain low. Inflation continued to mount, with the CPI estimated 6.6% higher than a year ago in Q4, and the Fed's preferred core measurement up 4.4%. With costs rising,

5075 Shoreham Place, Ste 120 San Diego, CA 92122 858-558-3600/ fax 858-952-5886 www.DenaliAdvisors.com

quarterly profits for the S&P 500 are estimated to have dropped slightly in Q4, and are forecast to rise at a mid-single-digit percentage for the next two quarters.

The FOMC began tapering their asset purchases, and 10-year Treasury yields approached 1.7% in October and November, but fell sharply to under 1.4% in early December as the emergence of omicron spooked markets. As those fears eased and the Fed signaled multiple rate increases for 2022, yields recovered to end the quarter unchanged at 1.52%. Oil prices followed a similar path, with little net change over the quarter. The resumption of faster growth powered US stocks to strong gains in the fourth quarter. The Russell 3000 index gained 9.28% for the quarter and 25.66% for the year 2021. The very largest tech stocks remained highly valued by investors, and Growth outperformed Value among the 200 largest stocks by over 6%. However, Value outperformed by a wide margin in every other market cap stratum, over 4% in the Russell 2000. This pattern also held for the year as a whole, but by even wider margins. Volatility in the relative performance of the Russell 1000 style indexes remains near its highest in 20 years. Meanwhile, the Russell 1000 outperformed the small cap Russell 2000 for a third quarter running, by 7.6% in Q4.

We expect the heightened volatility of Value vs. Growth performance to continue, while over time we expect to see Value taking two steps forward and one step back vs. Growth. We are now seeing the winding down of extreme accommodation in monetary policy. Inflation expectations and interest rates turning up from very low levels will continue to benefit Financials (heavily represented among both Value and small cap stocks) and pressure high valuation multiples. The tech giants really have had stellar earnings performance, but they remain priced at high (in some cases enormous) multiples of those earnings. With the tide of interest rates rising for a long time to come, and the pandemic impacts to the in-person economy receding, it seems doubtful that they can continue to drive Growth returns ahead of Value. The historically very high valuation differentials between Growth and Value and between large and small cap stocks that had persisted for several years before this recent accelerated market cycle have begun to revert toward normal levels. We expect to see this continue and eventually penetrate that largest market cap level. Normalizing markets have generally been friendly to valuation-oriented strategies, and we have seen this in the outperformance of our strategies this quarter and year. We expect this favorable environment to continue for some time to come.

Denali Network Value Small Disclosures

Returns are presented gross and net of management fees and include the reinvestment of all income. Actual investment management fees are used to calculate net of fees returns unless otherwise noted in the composite specific disclosures. Past performance is not indicative of future results.
Denali Advisors, LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Denali Advisors has been independently verified for the periods April 1, 2007 through June 30, 2021. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report. Denali is an independent registered investment advisor. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Denali was established in 2001 and manages equity and alternative assets for primarily institutional clients. The U.S. dollar is the currency used to express performance. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year. Leverage is not used. Additional information regarding Denali's policies and procedures for valuing portfolios, calculating performance and preparing GIPS Reports available upon request. The firm's list of composite descriptions is available upon request. Please contact Anne Erickson at Anne@DenaliAdvisors.com.

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Denali Network Value Small: Composite consists of fully discretionary small cap portfolios. Results are compared against the Russell 2000 Value and intend to outperform that benchmark while maintaining similar sector, industry and security characteristics. The Denali Network Value Small Composite inception and creation date is June 01, 2013. As of February 18, 2016, the secondary benchmark Russell 2000 was removed as it is no longer representative of the strategy. The NV Small portfolio construction is based on the analysis of earnings, liquidity and other characteristics of selected companies from the Russell 2000 index. The composite was comprised of 100% non-fee-paying accounts for periods presented through March 31, 2019, net returns were calculated by reducing gross monthly returns by a model management fee of 1%. As of April 1. 2019 the net returns have been calculated using actual management fees. The management fee for this product is 1.00%. Client returns will be reduced by advisory and other expenses the client may incur. There is a marketing minimum of $1 million.
*Network Value Small Index: The results presented reflect research returns of a historical simulation of the construction process for the Denali Network Value Large index beginning at the end of December 1994 and tested through April 2013, combined with the results of index portfolios constructed contemporaneously each month from May 2013 through the most recent month-end. Index portfolios were rebalanced as of the end of each month of the historical period using historical data available at the time as input to Denali's proprietary Network Value index construction process. The security selection universe was the membership of the Russell 2000 index, which is meant to represent the investable small cap stock universe in the United States. Data used in the historical simulation was sourced from Compustat, and the Barra U.S. Equity model was used for performance calculation. Real time performance presented for periods since May 2013 is without the benefit of hindsight in model development. This Index is not offered as an investment vehicle and like all indexes is not directly investable; the returns do not account for any transaction costs of rebalancing.

Denali Network Value Small		Composite Assets		Annual Performance Results				3-Year Annualized Standard Deviation*	
Year End	Total Firm Assets (millions)	US Dollars (Millions)	Accounts in composite	Composite Gross	Composite Net	Russell 2000 Value	Composite Dispersion	Composite	Benchmark
2020	729	197	Five or Fewer	3.60%	3.19%	4.63%	N.A.	25.65%	26.49%
2019	1,338	116	Five or Fewer	24.01%	23.42%	22.39%	N.A.	15.16%	15.90%
2018	1,401	Less than a million	Five or Fewer	-5.89%	-6.85%	-12.86%	N.A.	14.93%	15.98%
2017	1,311	Less than a million	Five or Fewer	5.83%	4.79%	7.84%	N.A.	14.67%	14.17%
2016	762	Less than a million	Five or Fewer	28.85%	27.64%	31.74%	N.A.	16.48%	15.72%
2015	476	Less than a million	Five or fewer	-2.58%	-3.56%	-7.47%	N.A.	N.A.	N.A.
2014	357	Less than a million	Five or Fewer	8.53%	7.47%	4.22%	N.A	N.A	N.A
6/01/2013 - 12/31/2013	323	Less than a million	Five or Fewer	24.60%	23.94%	17.12%	N.A.	N.A.	N.A.

*3-Year Annualized Standard Deviation and Composite Dispersion is calculated using gross of fees returns. N.A. means an insufficient number of portfolios or insufficient number of periods.