Denali Network Value Small
1Q 2021 Commentary

- Our **Network Value Small** composite gained 21.55% in Q1 (gross of fees), edging past the benchmark Russell 2000 Value Index's strong gain of 21.17%. Since the pandemic crash, in the past year Denali's portfolio has returned 97.85%, vs. 97.05% for the benchmark.
- The relation of returns to reported earnings was complex. The quintile of stocks with highest earnings relative to price outperformed at 24%, but that with the ***largest losses*** gained twice as much at 48%. Investors evidently viewed some pandemic-induced losses as one-offs. Our position favoring higher E/P quintiles still added about 30 bp active return.
- As in Q4, our overweight in smaller cap (lower liquidity) stocks again added significantly to our active performance.
- Our Network Value Index, focused on stocks with both higher earnings and lower liquidity, gained 20.8%, slightly behind the benchmark but 9.1% above the broad Russell 2000.
- The stock-level Network Value forecast had very positive predictive performance and our intrinsic value model better still, consistent with the favorable environment for Value. Our Detailed Estimates forecast results were also strong. Characteristics Trend forecast results were only neutral amid prevalent factor momentum reversals the past six months.
- Linear attribution shows exposure to higher reported earnings/price was the worst detractor from active return, but forecast E/P was most positive and other valuation ratios (Sales, Book Value) were strongly beneficial, as was lower average momentum. Our slightly lower beta and small cash holding slowed return by 140 bp. Lower relative liquidity, lower volatility in both price and earnings, and higher Coverage Ratio detracted significantly, net of other factor effects.
- GICS sector allocation produced half of active return; underweights in defensive Utilities, Real Estate and Health Care helped, but those in Energy and Discretionary detracted. Selection within sectors was strong in Financials (banks), Staples (retail), Energy, Tech and Industrials, but adverse in Materials, Discretionary (no Gamestop!) and Health Care.

Market Outlook

The investment environment is of course still heavily influenced by the course of the Covid-19 pandemic, which is developing rapidly. Vaccination of large numbers of the most vulnerable segments in the U.S. population pulled down Covid cases and death rates very rapidly in January and February. Although reported infection numbers leveled off in March, death rates continued to decline. As a result, the U.S. economy continued to recover strongly as restrictions and risks abated; the consensus estimate compiled by Bloomberg is that GDP grew at a 4.7% rate in the first quarter. The main driver of economic developments is now shifting from the disease itself to government actions, partly in response to the pandemic and partly to the policy preferences of the new governing party. These actions combine very loose monetary policy, positively seeking to drive up inflation, with huge fiscal stimulus in the form of deficit spending. Accordingly, GDP is forecast to grow at nearly 7% rate for the next two quarters. Consequently, long-term interest rates have risen strongly, with the 10-year Treasury yield up 80 bp to 1.74%. Quarterly profits for the S&P 500 are estimated to have regained pre-pandemic levels in Q1, with a 15% rise predicted by Q3. In response, the U.S. equity market again rose to new record highs. The Russell 3000 Index gained 6.4% in Q1 and 63% for the trailing year, its best four-quarter run since 1983. Better results for economically sensitive companies and less disadvantage for the in-person economy vs. the virtual pushed Value and small cap stocks ahead again in the quarter. But whereas in Q4 the outperformance of less liquid / smaller cap stocks was the stronger effect, while higher P/E stocks still outperformed, in Q1 performance shifted strongly in favor of stocks with less expensive prices relative to fundamentals, especially earnings. Within the small caps in particular, the Russell 2000 Value index led Growth by 16%, the second-biggest margin ever.

We expect both of these relative performance trends, favoring Value and less liquid / smaller stocks, to continue in the medium term. Inflation expectations and interest rates turning up from very low levels will benefit Financials (heavily represented among both Value and small cap stocks) and pressure high valuation multiples. The historically very high valuation differentials between Growth and Value and between large and small cap stocks that have persisted for several years before this recent accelerated market cycle have only just begun to revert toward normal levels. Normalizing markets have generally been friendly to valuation-oriented strategies.

With slower evolution in macroeconomic expectations, we would expect less exaggerated movements in the level of the markets, as was the case in Q1. However, we expect volatility to remain relatively high. One reason is that significant policy uncertainty will persist, including regarding changes in tax rates and regulations. Also, we continue to think that the expected (or dreamed-of) growth rates built into the valuations of the most influential Growth stocks must come down to more realistic levels in the medium term, and that adjustment process is unlikely to be smooth.

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

Denali Network Value Small GIPS Composite Report

Performance numbers presented on pages A-1B.
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 December 31, 2020. 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.

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 $5 million.

Denali Network Value Small		Composite Assets		Annual Performance Results				3-Year Annualized Standard Deviation*	
				Composite					
Year End	Total Firm Assets (millions)	US Dollars (Millions)	Accounts in composite	Gross	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.