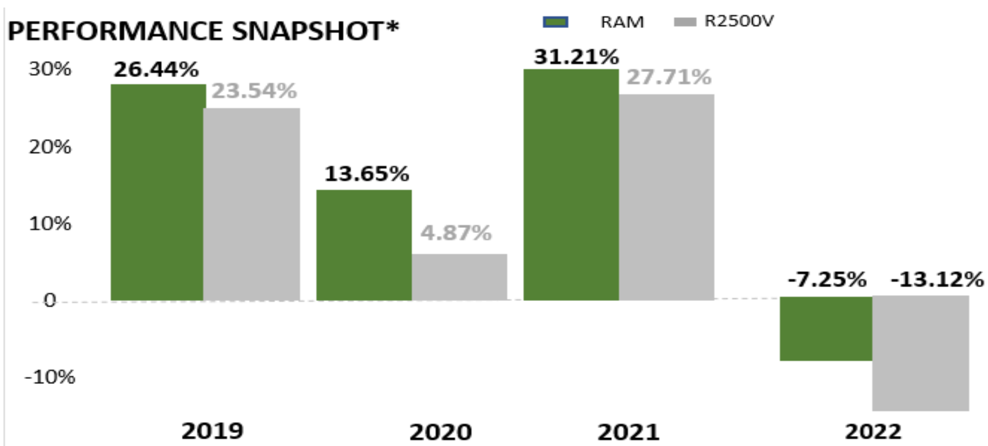
January 2023

While the major equity indexes shook off the 3Q22 stock swoon to rally in 4Q22, the combined pressures of Fed rate hikes, recession fears and continued supply chain snafus led most major indexes to a negative return for the year. The Russell 2500 Value index (R2500V) rallied strongly off its intra-year low set on September 30th (the 3Q22 close), to finish up 9.2% for 4Q22, but down 13.12% for 2022. For the year the S&P500 fell 18.17% and the Nasdaq fell 32.51%. We were pleased with the performance of our RAM Smid cap strategy, which gained 16.25% in 4Q22, 7.05% ahead of our R2500V benchmark, and finished the year down 7.25%, 5.87% ahead of the R2500V.[1,2]



Source: Rewey Asset Management, Index returns sourced from Bloomberg 12/31/2022.

Please note that there are material limitations inherent in any comparison between RAM Smid strategy and the R2500 Value Index. The R2500 Value Index is unmanaged and you cannot invest directly in an index. The RAM portfolio is actively managed and holds concentrated investments in the equity securities of small-mid capitalized companies.

Fed "Strongly Committed" to 2%

The Fed was the highlight of the fourth-quarter and indeed all of 2022. On December 14, the Fed raised Fed funds rates for the seventh time in 2022 to a range of 4.25%-4.50%, an increase of 50 basis points, after four successive meetings with 75 bps each. The resultant 4.25%-4.5% Fed funds rate target is unprecedented in its speed of hikes, up from zero before the March 16, 2022 meeting. We have written extensively in our blogs and quarterly letters that we believed the Fed would have to move aggressively to tame rampant inflation, after waiting too long to abandon its flawed 'transitory' inflation views. At the December meeting, Chairman Powell once again affirmed that the Fed is strongly committed to its 2% inflation goal. Concurrent with this meeting, the Fed released its projections that showed further expected hikes in 2023 to a peak of 5.1%, before cuts could be expected in 2024. These rate cuts, are predicated on the Fed's view that inflation continues to fall to its 2% goal, ending 2023 at 3.5%, at 2.5% for 2024 and 2.1% in 2025.[3,4]

Walking the Line – Can the Fed Achive a 2-Step Reduction?

We would not put too much faith in the Fed's expected path, as its expectations changed radically in 2022, and are likely to continue to be volatile in 2023 and beyond. What we see as the important take-away, besides the commitment to continue rate hikes in 2023, is the view that the U.S. economy will not enter into recession in 2023-2025, with GDP expectations set at 0.5% for 2023, and then rising to 1.6% in 2024 and 1.8% in 2025. The Fed essentially, is projecting that it will successfully be able to walk the line to a soft-landing while breaking inflation.

In our 3Q22 letter we noted that the current economic conditions did not reflect any recession we have witnessed, and we maintain this stance today. In speaking with our companies, we still see strong consumer and business demand, and a continued inability to fill this demand due to supply chain shortages. We think current conditions are in the Fed's favor for 2023 to achieve the 'first-step' of falling inflation and a soft landing, driven by supply chain stabilization and the reversion of supply constrained price hikes, as deferred consumer demand is backfilled to sales and finished goods inventory levels are rebuilt. This first-step will likely be much easier to achieve than the second-step. To achieve what we think is the second-step of inflation reduction, the Fed will need to tame higher wage inflation and real estate/rental inflation and achieve a lasting soft landing. In our view, if the Fed wants to break inflation back to 2%, wages and jobs will need to suffer, and thus it is much harder to agree with accelerating GDP growth for 2024 and 2025. The results of this 2-step Fed battle will likely dominate financial headlines for 2023.

Luckily, from our perspective, this battle has little impact on our view of the potential upside of our 26 position portfolio. We have selected companies with low debt and good debt service coverage, that we think can withstand higher interest rates, and are able to implement price increases.

The Return of Value Outperformance

The other major story of 2022 was the outperformance of the value Indices vs. their growth peers across all market capitalizaitons. We had written in our Market Musing blogs and our quarterly letters that in our view rising rates would lead to reduced valuation levels for growthier stocks, especially those with no near-term cash flow and valuation targets overly reliant on the 'terminal value' of a discounted cash flow (DCF) model. Simply, if the discount rate is raised, longer duration cash flow streams are negatively impacted compared to more visible near-term cash flow streams.

While higher rates negatively impacted valuation levels for the market as a whole, we saw value indices greatly outperform their growth peers. The table below shows this value vs. growth outperformance across all market cap segments. We also include the S&P 500 ETF to illustrate our view that this index has for years skewed to the growth style.[5]

	Index Returns	
	4Q22	2022
Russell 2000 Value	8.39%	-14.50%
Russell 2000 Growth	4.11%	-26.39%
Russell 2500 Value	9.20%	-13.12%
Russell 2500 Growth	4.70%	-26.22%
Russell Large Cap Value	12.40%	-7.56%
Russell Large Cap Growth	2.19%	-29.14%
Russell All Cap Value	12.16%	-8.01%
Russell All Cap Growth	2.31%	-28.97%
S&P 500 (SPY)	7.57%	-18.17%

Source: Bloomberg

Value vs. Growth: We Think the First Inning Just Ended

We think the outperformance of the value style vs. the growth style will continue throughout 2023, and likely beyond, i.e. we are in the early innings. Our view continues to be that the quantitative easing (QE) policies of the Fed to keep interest rates near zero supported a period that rewarded businesses models that produced low or no cash flows and were overly reliant on external equity funding, both from equity offerings and employees who were paid in stock versus cash. With the Fed intent on raising rates until inflation breaks, we see the unraveling of these untested and highly valued business models. Conversely, for the most part, value style equities have strong balance sheets and cash flows that support current operations without external funding, and valuations that are more in line with pre-QE levels.

The Return of a Stock Picker's Market

While we see a favorable environment for the value style, we are not suggesting broad index buying as a strategy. Our RAM philosophy incorporates not only financial strength as our first pillar and compelling valuation as our third pillar, but also a view that a successful company must have the 'ability to grow', our second pillar. We don't define value investing solely on the retroactive measure of book value. We have also never believed that value was the antonym of growth, and we believe that value companies that can't grow are the classic examples of value traps. With the increased macro headwinds of Fed rate hikes, low levels of GDP growth and persistent pockets of inflation, we believe active due diligence and analysis will be necessary to select stocks that can outperform today's investment headwinds.

Portfolio Highlights

We believe our RAM Smid portfolio is well positioned for rising rates and moderating inflation, and is also very attractive from a valuation perspective. Focusing on the balance sheet, five holdings are trading under book value and eight additional holdings are trading at less than 1.5x book. We have also focused on companies with low leverage. By our estimates, 15 of our 22 non-bank holdings have less than a 1x 2023(e) Debt/EBITDA ratio. Further, only two have materially over a 3x ratio, and while we believe debt service is not material risk for these two positions, together they account for only approximately 4% of the total portfolio. It is also worth highlighting that four of our holdings have no sell-side coverage, and nine others have five or fewer covering analysts. We believe this anonymity provides us with the opportunity to identify companies that pass under the radar for other investors, and help secure positions at attractive valuations.[6,7] At quarter-end, our RAM Smid cash level averaged slightly over 9.0%[8]. We added four new companies to the portfolio in the quarter, and sold out four positions, inclusive of the Orthofix/SeaSpine Holdings tax swap.

Mayville Equipment Corporation (MEC) was RAM Smid's top percentage gainer in the quarter, up 94.43%. It mattered when it mattered for investors in the quarter, as shares rallied strongly post its November 2nd earnings call. While in our view there was not much new information on the call, management did review and reaffirm the strengths of MEC, including its balance sheet, its accelerating margin potential, its potential for revenue growth from 'reshoring', the productivity enhancement programs the new CEO is implementing and the irrelevance of the lost Peleton work that never actually started. We still see substantial upside potential for MEC, and note that management unofficially raised its operating margin target range to 18% vs. a prior 15% at the the Sidotti conference in December.[9]

Petco Health and Wellness (WOOF) was RAM Smid's largest detractor in the quarter, falling just over 15%. Shares sagged as investors feared the impact of rising interest rates on its debt, as well as the 3Q22 management commentary about slowing low-end consumable demand. We believe with the new interest rate caps in place for 2023 and 2024, as well as strong cash flow, WOOF will be able to reduce debt levels and invest in the business. Further, we continue to believe in the "furry annuity" of pet adoptions. Despite fears of a decline, pet adoptions remain strong and relinquishment rates are under pre-pandemic levels. WOOF's trifecta of service offerings of veterinary care, in-store grooming and shopping and internet delivery are well suited in our view to prevail over single product offering focused competitors. We see sustained revenue growth powered by WOOF's Vital Care membership rewards program, its growing in-store veterinary hospital count, and continued strength in premium products, including its rapidly growing refrigerated fresh food offerings.[10]

Skyworks Solutions Inc. (SWKS)

We continued to build our position in Skyworks Solutions Inc. (SWKS) in the quarter, a $14.68 billion market cap company that specializes in designing and producing microchips for communication including 5G, Wifi, and other RFID technologies. SWKS's chips are broadly used in any device requiring wireless communication, including cellular handsets, data centers, home networks and self-driving cars.

Shares of SWKS remain near our initial September purchase levels, as investors fear the short-term impact of broad semi-conductor weakness globally, Chinese handset volume softness and concerns about delays in the production of the new Apple 14 series iPhones. We believe these fears are adequately reflected in the current stock price as SWKS has lowered its near-term China sales estimates to zero and regardless of any short-term iPhone bumps, we think the iPhone remains the dominant high-end technology that consumers will wait for, versus switching to other platforms. Moreover, the long-term outlook for SWKS, in our view, is compelling due to growth in the internet of things (IOT), self driving car technologies and continued demand for technology intensive hadset devices.

Skyworks easily meets our definition of having a strong balance sheet, the first parameter of our investment philosophy. At its FY22 year end (Sept.), SWKS had $586 million of cash on the balance sheet, and net debt of roughly $1.6 billion dollars, representing about .72x our 2023 EBITDA estimate and about 1.0x our estimate of free cash flow for FY2023. Over the last few years, SWKS has used its strong free cash flow to make acquisitions, reduce debt and aggressively repurchase stock ($886 million repurchased in FY22, with over $1.0 billion remaining on its authorization). SWKS also has aggressively raised its dividend since inception in 2014, including a 10% hike in FY22 and 12% in FY2021, and at year-end had a dividend yield of 2.72%.

Skyworks should benefit from the long-term industry growth driver of increased wireless data traffic and consumption, not only in handsets, but in the high-growth emerging areas of the Internet of Things (IOT) and automotive communications, including self-driving ADAS systems. Skyworks invests roughly 11% of its annual revenues to research and development to fund growth into these and other areas.

In the wireless network area, SWKS should benefit from the continued transition to wifi 6/6e and the emergence of wifi 7 in late 2023. Wifi grow will likely be powered by the continued growth of machine to machine communication (IOT) and home and office network growth, including security and climate solutions. Also, supported by its July 2021 acquisition of the Infrastructure and Automotive business of Silicon Labs, SWKS should see accelerating growth into cars, especially EV's and self-driving ADAS systems. SWKS notes that a self-driving ADAS vehicle uses approximately 25-times the data of a high-end handset.

We believe the valuation opportunity for Skyworks is compelling. At its year-end close of $91.13, SWKS is trading 44.25% under its 2022 high of $163.47, a clear sign that investors are well aware of the near-term revenue headwinds. At this price, we believe SWKS suffers from substantial investor fear and neglect, trading at just over a 9x PE ratio 7.4x EV/EBITDA on 2023 street estimates, which in our view reflect current handset expectations. We believe investors are not only ignoring the long-term growth prospects of SWKS, but also the free cash flow power the company possesses. Combined with strong margins, low debt, and CAPX requirements that are only slightly higher than depreciation, we see Free Cash Flow approaching $1.6 billion in FY2023, representing a strong FCF yield of 10.89% at year-end.

With this strong cash flow, we believe SWKS can continue to invest in internal R&D, as well as continue to reduce debt, repurchase shares and seek M&A transactions. We have set our Adjusted Fair Value (AFV) price target at $126, 38% above its year end close, in addition to its 2.72% dividend yield. Our AFV is set off PE of 12.5x and EV/EBITDA of 10x, both at the low-end of historical ranges (PE 10x-25x and EV/EBITDA 8x-18x).

While we do not incorporate any upside from a potential take-over of SWKS into our estimates, we see a better than average chance that a larger semiconductor company would be interested in SWKS mobile offerings, especially as many of these companies face slowing demand in mainline chips in the gaming and PC sectors. [11]

Looking Forward

As we look forward into 2023, we caution investors not to put too much faith in economic forecasts from the sell-side firms. First, these forecasts are quite often wildly off the mark (recall, at this time last year most believed rates would stay low and inflation was transitory). We sometimes joke that these economists make one annual forecast, and 51 weely revisions.

More importantly, we don't own the market. We own 26 companies with well defined investment cases, built off strong balance sheets, visible growth scenarios and what we believe are significantly positive risk versus reward valuation characteristics. We have selected companies with low and manageable debt levels and where we see pricing power to overcome inflationionary headwinds.

We thank you for your trust and support. As always, please do not hesitate to contact us for client service, to discuss our commentary or to simply opine on the market and stocks.

-Chip

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1. Past performance is no guarantee of future results. The RAM SMID Value Composite schedule of net investment performance of Rewey Investment Management LLC (the "Schedule") represents the activity of separate customer trading accounts managed collectively (collectively the "Accounts") for the annual and cumulative periods from January 1, 2019 through December 30, 2022. 2022 performance unaudited. Please see full Marcum footnotes for RAM Smid composite 2019-2021 at Microsoft Word - {A44BB912-3141-4B59-AE8E-3D695C6B8BD4} (reweyassetmanagement.com). Performance graphic not to scale.

2. The Russell 2500 Value, the S&P 500 and Nasdaq Composite Index performance levels are sourced from Bloomberg. The Russell 2500 Value, S&P 500 and Nasdaq Composite indicies are an unmanaged group of securities considered to be representative of the small and mid-cap stock market, and the large-cap stock market in general, respectively. Indexes are unmanaged and do not incur management fees, costs, or expenses. It is not possible to invest directly in an index. There are material differences between the RAM SMID Value Composite portfolio and the indexes used for comparison purposes. The RAM portfolio is actively managed and holds concentrated investments in the equity securities of small-mid capitalized

companies. An index is generally designed to illustrate the performance of a specific asset class (i.e. small cap), but is not actively managed and the index performance does not reflect the impact of advisory fees and other investment costs.

3. U.S. Federal Reserve FOMC Statement 12/14/22 Federal Reserve Board - Federal Reserve issues FOMC statement

4. U.S. Federal Reserve 12/14/22 projections The Fed - December 14, 2022: FOMC Projections materials, accessible version (federalreserve.gov)

5. The Russell 2000 Value, the Russell 2000 Growth, the Russell 2500 Value, the Russell 2500 Growth, The Russell 1000 Value, The Russell 1000 Growth, The Russell 3000 Value and The Russell Growth and the S&P 500 Index performce levels are sourced from Bloomberg. All of these indicies are individually an unmanaged group of securities considered to be representative of the specific market-cap segments of the broader stock market. Indexes are unmanaged and do not incur management fees, costs, or expenses. It is not possible to invest directly in an index. An index is generally designed to illustrate the performance of a specific asset class (i.e. small cap), but is not actively managed and the index performance does not reflect the impact of advisory fees and other investment costs.

6, 8. All portfolio discussion is based off our model RAM Smid portfolio of separately managed accounts. Company financial estimates sourced from Rewey Asset Management proprietary analysis, and Bloomberg BEST company estimates. Historical pricing and company financial data sourced from company 10Q and 10K filings, and Bloomberg. Individual portfolios may hold slight deviations in position sizes, cash levels and positions held.

7. Covering active sell-side analyst data sourced from Bloomberg.

9. Mayville Engineering Company, Inc. (MEC) quarterly performance information sourced from Bloomberg. Other MEC commentary sourced from company earnings releases, 10Q, 10K filings, company presentations, RAM discussions with management, Bloomberg and Rewey Asset Management proprietary analysis.

10. Petco Health and Wellness Co., Inc. (WOOF) quarterly performance information sourced from Bloomberg. Other WOOF commentary sourced from company earnings releases, 10Q, 10K filings, company presentations, RAM discussions with management, Bloomberg and Rewey Asset Management proprietary analysis.

11. All financial ratios, statistics, and projections discussed in the Skyworks Solutions Inc. (SWKS) commentary are sourced from SWKS 10-K and 10Q filings, company press releases, company public conference calls and webcasts, company slide presentations, SWKS company webpage, RAM discussions with SWKS management and Rewey Asset Management proprietary financial analysis and Rewey Asset Management industry due diligence. Historical share price information sourced from Bloomberg.

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