AMG GW&K Small Cap Value Fund

COMMENTARY — ASSET CLASS | SMALL CAP

Class N | SKSEX — Class I | SKSIX — Class Z | SKSZX

GW&K INVESTMENT MANAGEMENT

Average Annual Returns (%)[1] (as of 09/30/21)

	Q3	YTD	1 yr	3 yr	5 yr	10 yr	Since Incpt.
SKSEX (Class N)	0.75	23.65	57.21	9.28	10.63	14.00	11.66[2]
SKSIX (Class I)	0.81	23.80	57.55	9.47	—	—	8.30[3]
SKSZX (Class Z)	0.84	23.86	57.58	9.55	—	—	8.38[3]
Russell 2000® Value Index	-2.98	22.92	63.92	8.58	11.03	13.22	—

SKSEX (Class N) Expense Ratio (Gross/Net)[4]: 1.18%/1.15%

SKSIX (Class I) Expense Ratio (Gross/Net)[4]: 0.98%/0.95%

SKSZX (Class Z) Expense Ratio (Gross/Net)[4]: 0.93%/0.90%

The performance data shown represents past performance. Past performance is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. The investment return and the principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. For performance information through the most recent month end, please call 800.835.3879 or visit our website at amgfunds.com. From time to time the advisor has waived fees or reimbursed expenses, which may have resulted in higher returns.

The **AMG GW&K Small Cap Value Fund** (Class N) returned 0.75% in the third quarter of 2021, compared with a -2.98% return for its benchmark, the Russell 2000® Value Index. For the 12-month period ending September 30, 2021, the Fund returned 57.21% compared to a 63.92% return for its benchmark. Please note that this Fund has multiple share classes.

The harder they come, the harder they fall. While AMC Entertainment (AMC) and other meme stocks would have seemingly little connection to the 1972 Jimmy Cliff song and movie of the same title, the third-quarter stock market action provides an unlikely and unexpected link. Struggling to build something out of nothing, the meme stock group came at markets hard with outsized moves in January and May/June of this year. A few traders made a huge payday and many more joined the game seeking easy wins, not realizing the structure of an investment bubble meant the odds were stacked against them. Ultimately these stocks must fall, as the weight of their inflated size becomes too great to maintain or expand. AMC experienced that hard fall in the third quarter, dropping -33%, with many other meme stocks following in direction if not in magnitude. Most traders involved in the space will come away with nothing and some lose their shirts. Like the hero early in the film, these traders are operating in a system they don't fully understand, and this system seems stacked against them. Investment success is much more likely when one takes a long view. Investors fall hard when they attempt strategies looking for quick and easy success.

For the small cap universe overall, the third quarter was similarly negative. While AMC lost a third of its value, the Russell 2000® merely declined (-4.4%) and lagged large caps. The Russell 2000® Value (-3.0%) outperformed the Russell 2000® Growth (-5.7%) in the quarter by almost 270 bps as cyclicals and financials generally performed better than areas of stable or speculative growth. The high for the Russell 2000® during the quarter was on July 1 and the index has made no progress since early February. Investors of all types might be asking, what exactly is the problem with U.S. small caps? We will attempt to offer a more complete answer, but in some ways the meme stock influence has been a weight on the benchmark. U.S. small caps were bid up as a marker for domestic cyclical growth coming off the pandemic lows, and speculative furor made its greatest impact down market cap. Some of these gains needed to be digested or wrung out. AMC itself was responsible for over 6% of the decline in the Russell 2000® and over 15% of the decline in the Russell 2000® Value in the third quarter, with other smaller memes pitching in as well. Meanwhile, outside of this meme world, a lot of strong businesses are seeing robust demand and delivering excellent earnings results.

Digging more into our benchmark's components for the quarter, we observe the inverse relationship between the meme stocks and higher quality companies. For the third quarter, stocks with lower price to earnings ratios, higher ROE, lower debt, higher yields, and higher earnings stability all outperformed the Russell 2000® Value Index. In fact, taking non-earners out of the benchmark would have reduced the Russell 2000® Value's decline to only -96 bps. On the sector side, higher oil and natural gas prices pushed the energy sector to the top position

[1] Returns for periods less than one year are not annualized.

[2] Since the inception of the Fund's Class N shares on April 23, 1987.

[3] Since the inception of the Fund's Class I and Z shares on February 24, 2017.

[4] The Fund's Investment Manager has contractually agreed, through at least May 1, 2022, to limit Fund operating expenses. The net expense ratio reflects this limitation, while the gross expense ratio does not. Please refer to the Fund's Prospectus for additional information on the Fund's expenses.

(+2.9%). Financials also ended the quarter positively (+2.0%), helped by earnings support and a hope for higher spreads between short and long interest rates. real estate (-1.0%) was an outperformer although slightly negative on the quarter. Communication services (-16.4%) was the worst performing sector, dragged lower by AMC and other stocks with limited earnings or cash flow support. Consumer discretionary declined (-8.4%) while health care (-6.7%) was hurt by its exposure to high secular growth stocks with a similar lack of earnings support. Materials (-4.8%), information technology (-4.6%), and consumer staples (-5.3%) were also lackluster performers.

The Fund outperformed its benchmark amid this environment. Stock selection broadly was solid, with particular strength in health care, consumer discretionary, and industrials. Strength in the health care sector was primarily from the 45% gain in Apollo Medical Holdings. An underweight position in biotechnology also contributed to relative outperformance as that industry declined (-6.1%) in the quarter. Within consumer discretionary, the Fund had three stocks with positive returns, even as the sector declined -8% in the quarter. These included Group One Automotive (+21.2%), Patrick Industries (+14.5%) and Boot Barn (+5.7%). In industrials, strong stock selection in the electrical equipment, airlines, and machinery industries drove relative performance. Two holdings in industrials were up double digits in the quarter, Atkore (+22.4%) and SkyWest (+14.6%). The decline in AMC also helped relative performance for the communication services sector, which added 65 bps of relative return in the third quarter. The only underperformance came from the energy and materials sectors. In energy, our underweight position worked against us as higher oil and natural gas prices drove share prices higher. In materials, stock selection in the metals & mining and chemicals industries drove relative underperformance. We had double-digit declines in three of our materials stocks, including Worthington Industries (-13.4%), Schnitzer Steel (-10.4%), and Materials Technologies (-11.2%). Nevertheless, the negative impact of these two sectors had a relatively modest impact on the quarter's results.

On the trading front, it was a fairly active quarter with four new holdings added and two holdings sold. The new holdings added during the quarter were in industrials (Terex (TEX), RBC Bearings (ROLL)), financials (PJT Partners (PJT)), and health care (SeaSpine (SPNE)). Terex is a manufacturer of aerial work platforms and materials processing machinery. We believe the company is well positioned to benefit from recovery tailwinds and should see additional growth opportunities from infrastructure legislation. RBC Bearings is a manufacturer and marketer of precision bearings and products used in the manufacture and operation of machines, aircraft, and mechanical systems. A selloff related to a share offering during the quarter provided an attractive entry point to start a positon in the stock. PJT Partners is an advisory-focused investment bank trading at a discount to its advisory/restructuring peers. SeaSpine develops spinal surgery technologies. We believe the company's new product innovation engine is underappreciated and should enable the company to outpace the market and take share. We also added to a number of names, including Allegiant Travel (ALGT), American Software (AMSWA), ProPetro (PUMP), and First Interstate BancSystem (FIBK). We sold two names that are being acquired, Lydall (LDL) and Flagstar Bancorp (FBC), and we trimmed two names following strong performance, Apollo Medical Holdings (AMEH) and Group One Automotive (GPI).

As mentioned above, the U.S. small cap market hasn't made much notional progress since early February of this year. While the composition of the benchmark is improving in both quality and valuation with the hard fall of meme and other low quality stocks and continued earnings strength from many other components, there are still a great many uncertainties for investors to consider. Or as Jimmy Cliff would say, there are Many River to Cross (amazingly, the B-side for the single The Harder They Come). The metaphorical rivers here include some waning fiscal support for the domestic economy, the partisan and even intra-party roadblocks in Washington, potential for Federal Reserve tapering or a market tantrum off of Fed speak or policy, supply chain shortages and challenges, and what appears to be an increasing acceptance of higher input prices, from commodities all the way up the value chain to labor. Will rising prices and interest rates result in a sudden change in the valuations investors are willing to pay for stocks? Could Delta or some other unknown variant change the calculus on our recovery from the pandemic? And we haven't even talked about China yet, which as the second largest economy in the world has domestic and foreign policy issues that could damage our best assumptions about future economic activity and corporate profits. Our conversations with small cap companies reveal demand that is still robust and creative thinking and innovation that can help circumvent many of these fundamental challenges. The risk of larger macro changes is always here. There are always rivers to cross. If we take the long view and avoid meme shortcuts, our probability of investment success will increase meaningfully.

The views expressed represent the opinions of GW&K Investment Management, as of September 30, 2021, are not intended as a forecast or guarantee of future results, and are subject to change without notice.

Top Ten Holdings (%)[5] (as of 09/30/21)

Holding	% of Net Assets
Tenet Healthcare Corp	2.58
Independent Realty Trust Inc	2.32
Piper Sandler Cos	2.22
Walker & Dunlop Inc	2.17
Group 1 Automotive Inc	2.15
Boot Barn Holdings Inc	2.12
Apollo Medical Holdings Inc	2.08
Gray Television Inc	2.03
Pacific Premier Bancorp Inc	2.00
Ameris Bancorp	1.98
TOTAL %	21.65

Disclosure

Investors should carefully consider the fund's investment objectives, risks, charges, and expenses before investing. For this and other information, please call 800.835.3879 or download a free prospectus. Read it carefully before investing or sending money.

Past performance is no guarantee of future results.

The Fund is subject to risks associated with investments in small-capitalization companies, such as erratic earnings patterns, competitive conditions, limited earnings history and a reliance on one or a limited number of products.

Companies that are in similar industry sectors may be similarly affected by particular economic or market events; to the extent the Fund has substantial holdings within a particular sector, the risks associated with that sector increase.

Market prices of investments held by the Fund may fall rapidly or unpredictably due to a variety of economic or political factors, market conditions, disasters or public health issues, or in response to events that affect particular industries or companies.

The Fund is subject to special risk considerations similar to those associated with the direct ownership of real estate. Real estate valuations may be subject to factors such as changing general and local economic, financial, competitive, and environmental conditions.

The Fund invests in value stocks, which may perform differently from the market as a whole and may be undervalued by the market for a long period of time.

The Russell 2000® Index is composed of the 2000 smallest stocks in the Russell 3000® Index and is widely regarded in the industry as the premier measure of small-cap stock performance.

The Russell 2000® Value Index is an unmanaged, market-value weighted, value-oriented index comprised of small stocks that have relatively low price-to-book ratios and lower forecasted growth values.

Unlike the Fund, indices are unmanaged, are not available for investment, and do not incur expenses.

Any sectors, industries, or securities discussed should not be perceived as investment recommendations. Any securities discussed may no longer be held in the Fund's portfolio. It should not be assumed that any of the securities transactions discussed were or will prove to be profitable, or that the investment recommendations we make in the future will be profitable.

AMG Funds are distributed by AMG Distributors, Inc., member FINRA/SIPC.

[5] Mention of a specific security should not be considered a recommendation to buy or a solicitation to sell that security. Holdings are subject to change.

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