



MARKETS

Equity markets paused in the second quarter with the Standard & Poor's 500 Index of large stocks returning 0.10% and the MSCI EAFE Index of developed international markets returning 1.56%. Caution was evident as small stocks, as represented by the Russell 2000 Index, gave up 1.61% and emerging markets, as represented by the MSCI Emerging Markets Index, gave up 1.15% for the quarter. With interest rates low, the search for income made Real Estate Investment Trusts a leading asset class for the quarter with a positive 2.94% return for the FTSE NAREIT Index. Investor preference for safety was also evident in the fixed-income markets with the Bank of America Merrill Lynch 3-to-5 Year Treasury Bond Index up 2.58% while the Bank of America Merrill Lynch U.S. High Yield Index was up only 0.99%.

THE ECONOMY

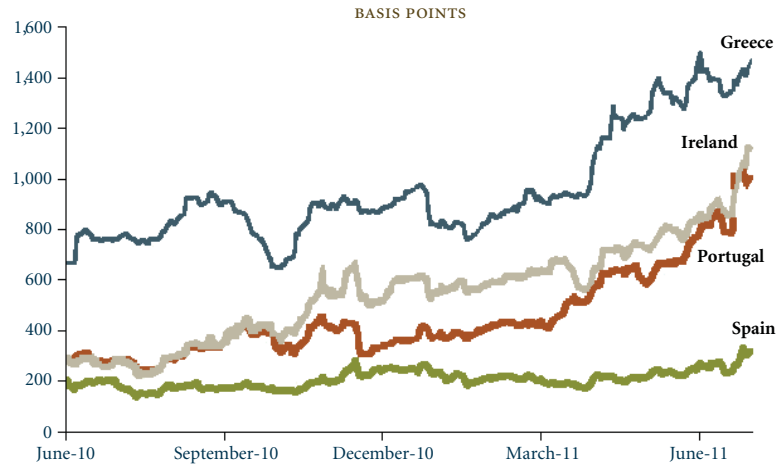
Despite overhanging issues requiring years of workout, we expect global economic growth to continue. The generational accumulation of household, State, and national debt means that growth will be restrained as evidenced in the current Congressional and White House discussions on lowering the budget deficit and slowing the rate of growth of the national debt. But, quite simply, there is no need for a recession. Recessions arrive in three forms: 1) Inventory recessions which last a fiscal quarter or two while inventories are worked down; 2) capital spending recessions which can take a year or more while the economy grows into an over-built infrastructure (think of the 2001-2002 recession following the technology boom); and 3) credit recessions, which are most difficult, that require debt to be restructured, having insufficient income to service it, and prices, having been leveraged up, to find new lower economic levels. This was the course of the Great Recession of 2008 and 2009. We are now two years into a painstaking recovery but inventories are lean, there has been no bulge in capital spending, and credit is available and cheap, all indications that we are not headed for a double-dip.

OVERHANGING ECONOMIC ISSUES

As referenced above, there are several issues that require attention in order for economic growth to continue. Among the most pressing issues are the following:

- ◆ Potential default in Greece
- ◆ The ending of QE2 on June 30, QE3 is not likely
- ◆ Short-term: The debt ceiling; Long-term: Debt/GDP is too high and rising
- ◆ The need for budget deficit reduction, fiscal de-stimulus
- ◆ Unemployment remains at elevated levels, which is an overhang on consumer spending
- ◆ Housing prices and construction activity remains weak

CREDIT DEFAULT SPREADS WITH GERMAN 10 YEAR



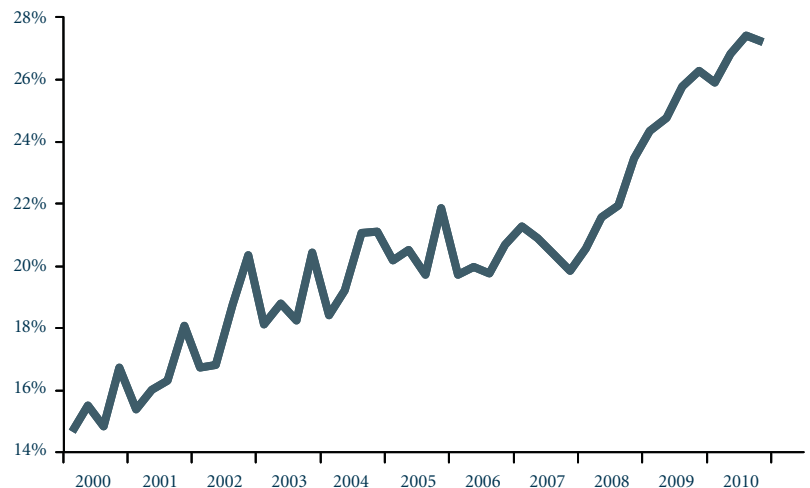
Source: Strategas Research Partners – Weekend Reader; Saturday July 16, 2011.
 Data reflect most recently available as of 6/30/11.
 Data is assumed to be reliable. Past performance is no guarantee of future results.

POSITIVES FOR ECONOMIC GROWTH

But, despite this overhang, we continue to believe that the economy will continue its modest pace of growth based on the following:

- ◆ Corporate cash is at an all-time high and is looking for investment opportunities
- ◆ Consumer balance sheets have improved
- ◆ Interest rates are unlikely to rise until unemployment is significantly lower
- ◆ The banking system is stronger capitalized and more liquid
- ◆ Japan is back to work

CORPORATE CASH AS A % OF CURRENT ASSETS
 S&P 500® COMPANIES — CASH AND CASH EQUIVALENTS, QUARTERLY



Source: Standard & Poor's, FactSet, and J.P. Morgan Asset Management
 Data reflect most recently available as of 6/30/11.
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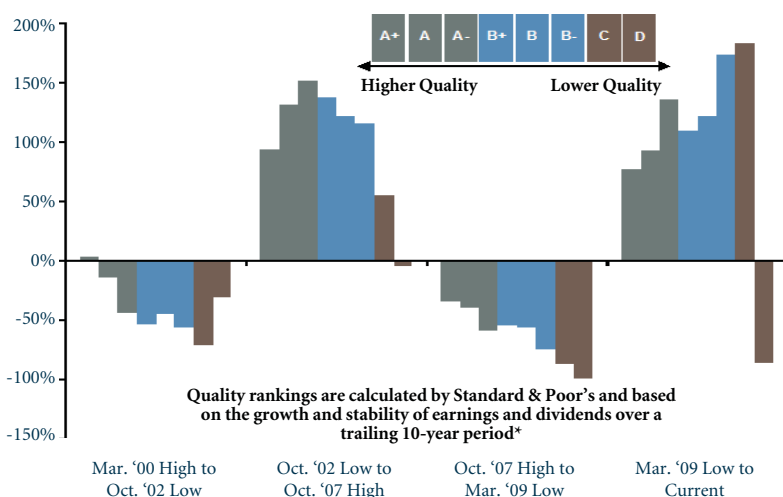
INVESTMENT OUTLOOK

We continue to believe that equity markets are a good place to invest. And, although fixed-income markets offer modest yield, they offer safety and stability with limited price risk from higher interest rates because of intransigent unemployment.

- ◆ Corporate America's seventh consecutive quarter of profit growth is a driver of equities and corporate bond credit.
- ◆ High unemployment and a break in commodities create profit-margin opportunity for equities and limit interest-rate risk in the fixed-income markets.
- ◆ Equity valuations remain attractive by historic measures both at absolute levels and relative to interest rates.
- ◆ With S&P 500 earnings expected to hit a new record this year, the S&P 500 Index remains approximately 15% below peak.
- ◆ With high corporate cash, increased M&A activity creates value for both acquirers and acquirees.
- ◆ In the modest growth economy we foresee, we believe high-quality businesses with protected markets are a better place to invest than lower quality companies operating in more competitive markets.

RETURNS BY STANDARD & POOR'S QUALITY RANKINGS

S&P 1500 INDEX CONSTITUENTS



Source: Standard & Poor's, FactSet, J.P. Morgan Asset Management.

Returns are based on beginning of period market capitalization weighted total returns and are calculated on a bottom-up basis. Quality buckets are based on beginning of period rating. Please note that companies without a quality ranking are excluded from calculations.

*For additional information on S&P's quality rankings, please see "Standard & Poor's Quality Rankings: Portfolio Performance, Risk, and Fundamental Analysis" from October 2005.

Data are most recent as of June 30, 2011.

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We encourage you to review your investment portfolio with your Kayne Anderson Rudnick advisor in order to prepare for the year ahead and assure a proper balance between preservation of capital and preservation of purchasing power. We recommend a conservative asset allocation that maintains a balance between stocks, bonds, and alternative investments that fits your unique income requirements and risk tolerance. We thank you for your continued confidence and we invite you to contact us with any questions or comments.

ORGANIZATIONAL UPDATE

We are pleased to announce the recent hire of Doug Foreman, CFA as Director of Equities. As Director of Equities, a new position for the firm, Mr. Foreman's responsibilities will be to evolve and advance the equity investment process, including the research tools used by the equity team, and to take the lead in product development. Mr. Foreman brings 25 years of industry experience to Kayne Anderson Rudnick.



ROBERT A. SCHWARZKOPF, CFA
 Chief Investment Officer

Robert A. Schwarzkopf, CFA, is Chief Investment Officer, a Portfolio Manager for the Small and Mid Cap Equity Portfolios, and a member of the Executive Management Committee. He has approximately 30 years of equity research experience.

The S&P 500® Index is a market capitalization weighted index which includes 500 of the largest companies in leading industries of the U.S. economy. The MSCI® EAFE Index is a free float-adjusted market capitalization index that measures developed foreign market equity performance, excluding the U.S. and Canada. The Bank of America Merrill Lynch High Yield Bond Index covers the U.S. dollar-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below. The FTSE NAREIT Index is a market capitalization weighted index of publicly-traded REITs in the U.S. The MSCI® Emerging Markets (EM) Index is a free-float adjusted market capitalization index tracking the equity performance of global emerging markets. The Bank of America Merrill Lynch 3-5 Year Treasury Index is a market value weighted index of short-term U.S. government securities with maturities between 3 and 5 years. The Russell 2000® Index is a market capitalization-weighted index of the 2,000 smallest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Performance is calculated on a total return basis with dividends reinvested. The indexes are unmanaged and not available for direct investment.

This report is based on the assumptions and analysis made and believed to be reasonable by Advisor. However, no assurance can be given that Advisor's opinions or expectations will be correct. This report is intended for informational purposes only and should not be considered a recommendation or solicitation to purchase securities. Past performance is no guarantee of future results.