Q2 21 AT THE TURN: MID-YEAR OBSERVATIONS

MARKET REVIEW AND OUTLOOK

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Equities continued to advance in the second quarter. Large-cap stocks, represented by the S&P 500® Index, appreciated 8.55%, bringing the year-to-date return to 15.25%. Large-cap growth outpaced large-cap value stocks, with the Russell 1000® Growth Index up 11.93% and the Russell 1000® Value Index up 5.21%. Year to date, however, large-cap value stocks remained ahead of growth stocks, returning 17.05% versus 12.99%, respectively. Small-capitalization stocks, as measured by the Russell 2000® Index, lagged their larger counterparts for the quarter with a return of 4.29%, but still slightly ahead year to date with a return of 17.54%. International equities continued to lag U.S. stocks. Developed markets equities, as measured by the MSCI EAFE® Index, were up 5.17% in the quarter and 8.83% year to date, and emerging markets equities, as measured by the MSCI Emerging Markets Index, were up 5.05% in the quarter and 7.45% year to date.

Despite improving economic conditions during the quarter, the 10-Year U.S. Treasury yield fell from 1.74% to 1.45%, surprising consensus expectations from three months ago of a continued rate rise.

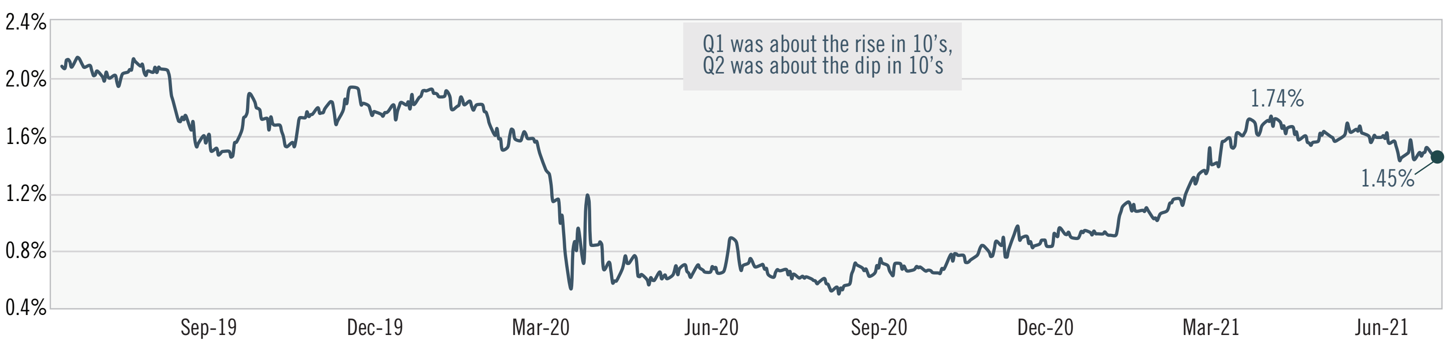
This decline in yields allowed the Bloomberg Barclays U.S. Aggregate Bond Index to advance 1.83% in the quarter, reducing the year-to-date loss to (1.60%). Spread-based fixed income performed well with high yield bonds, as measured by the ICE BofA U.S. High Yield Index, advancing 2.77% for the quarter and 3.70% year to date. Municipal bonds, as measured by the Bloomberg Barclays U.S. Municipal Index, advanced 1.42% for the quarter and 1.06% year to date.

WHY ARE LONG-TERM YIELDS FALLING IF INFLATION IS SUCH A THREAT?

Inflation hawks need to explain why long-term yields have fallen over the last three months despite improving economic activity, increasing mass vaccinations, and continued supply bottlenecks in many industries. Reasons provided, such as the foreign buying of U.S. Treasuries, quantitative easing by the Federal Reserve, or simple profit taking, do not seem to provide sufficient explanation. We believe that the best indication of long-term inflation expectations is the 30-year bond rate, which materially fell in the quarter from 2.41% to 2.06%.

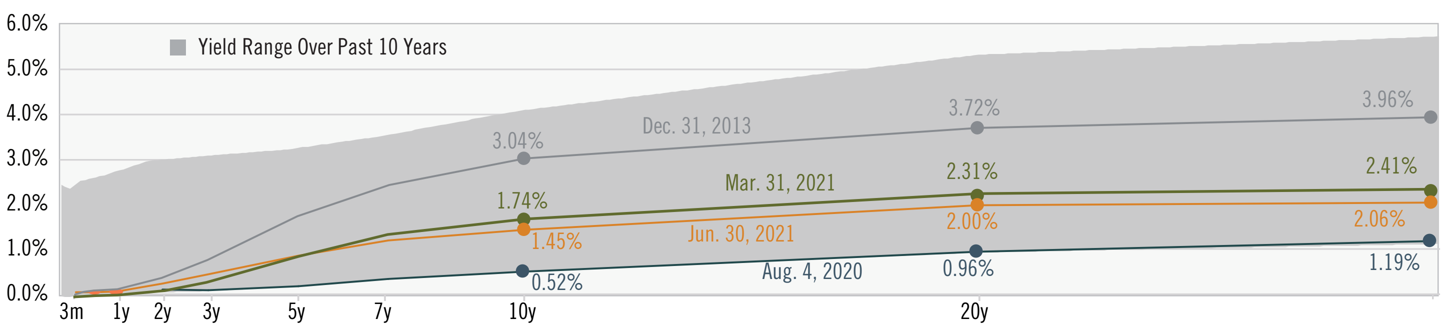
When investors speak of potential interest rate increases, it is important to understand which maturity they are referring to. The Fed only controls the very short end of the yield curve, and despite an expanding balance sheet of Treasuries held, they still don't control 10-, 20-, or 30-year rates. There are many historical instances of the Fed increasing short-term rates only to see longer-term rates actually decline as

FIGURE 1: 10-YEAR U.S. TREASURY YIELD



Past performance is no guarantee of future results. Data presented as of June 30, 2021. Data is obtained from Strategas and is assumed to be reliable.

FIGURE 2: U.S. TREASURY YIELD CURVE



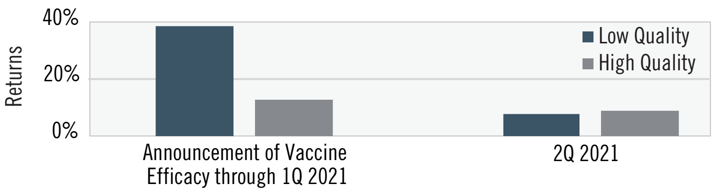
Past performance is no guarantee of future results. Data is obtained from FactSet, the Federal Reserve, and J.P. Morgan Asset Management and is assumed to be reliable. Forecasts are not a reliable indicator of future performance. Positive yield does not imply positive return.

the yield curve flattens or even inverts. So, while inflation data may appear well above the long-term trend of 2% over the balance of this year, we should expect to see more normal inflation data as we get into 2022.

IS THE LOW-QUALITY RALLY OVER?

Low-quality stocks tend to outperform at the bottom of a recession when economic activity is about to rapidly accelerate as the economy emerges from recession. This process started in early November 2020 when COVID-19 vaccine results of over 90% efficacy were announced. In the second quarter, low-quality stocks performed about in line with high-quality stocks, suggesting the stock market is anticipating continued growth. However, the rapid acceleration phase may already be behind us. Remember, the market is always trying to anticipate economic conditions over the next 6 to 12 months, and it seems likely that growth will continue but at a more moderate rate. Less fiscal support for individuals and increased taxes for corporations and high-income taxpayers seem like a virtual certainty and will clearly slow growth rates into 2022. It will be interesting to see over the next year if indeed low-quality outperformance has already run its course.

FIGURE 3: HIGH-QUALITY VS. LOW-QUALITY PERFORMANCE
Russell 3000® Index

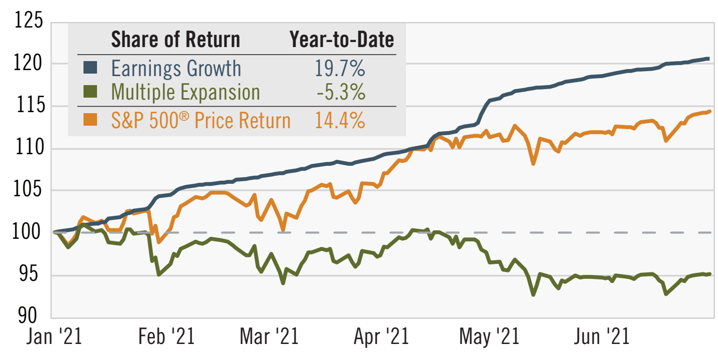


Past performance is no guarantee of future results. Announcement of vaccine efficacy date was November 6, 2020. Data is obtained from FactSet and is assumed to be reliable. Low Quality is represented by stocks with a beta of 2.0 and High Quality is represented by stocks with a beta of 0.5-1.0. Beta is a measure of a stock's volatility relative to the overall market. Higher beta suggests higher volatility.

WHAT SHOULD AN INVESTOR DO?

Despite elevated valuations, we believe investors should stay the course and remain invested. Price/earnings (P/E) ratios are higher than normal, but this is not unusual when earnings are rapidly recovering, and corporate earnings were nothing short of sensational in the first quarter. Ironically, P/E ratios may decline as the earnings recovery unfolds. However, as long as earnings growth exceeds multiple contractions, we believe returns should be favorable for investors. We also feel that having some balance between growth and value in a well-diversified equity portfolio is an important consideration at this point in the economic cycle as growth continues but moderates.

FIGURE 4: PERCENT CHANGE IN S&P 500®, EARNINGS AND VALUATIONS Year to Date, Indexed to 100



Past performance is no guarantee of future results. Data presented is as of June 30, 2021. Data is obtained from FactSet, Compustat, Standard & Poor's, and J.P. Morgan Asset Management and is assumed to be reliable. Historical EPS levels are based on annual operating earnings per share. Earnings estimates are based on estimates from Standard & Poor's and FactSet Market Aggregates.

In our proprietary equity portfolios, we will continue to purchase high-quality businesses regardless of the current economic regime. We believe competitive protections and differentiation are the key investment metrics that matter the most over the long term.

Authored by:

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Kayne Anderson Rudnick believes that superior risk-adjusted returns may be achieved through investment in high-quality companies with market dominance, excellent management, financial strength, and consistent growth, purchased at reasonable prices.

Index definitions: The **S&P 500® Index** is a market capitalization-weighted index that includes 500 of the largest U.S. companies. The **Russell 1000® Growth Index** is a market capitalization-weighted index of growth-oriented stocks of the 1,000 largest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. The **Russell 1000® Value Index** is a market capitalization-weighted index of value-oriented stocks of the 1,000 largest companies in the Russell Universe. The **Russell 2000® Index** is a market capitalization-weighted index of the 2,000 smallest companies in the Russell Universe. 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 **MSCI® Emerging Markets Index** is a free float-adjusted market capitalization index tracking the equity performance of global emerging markets. The **Bloomberg Barclays U.S. Aggregate Bond Index** is a market value-weighted index that tracks the daily price, coupon, pay downs, and total return performance of fixed-rate, publicly placed, dollar-denominated and non-convertible investment grade debt issues with at least $250 million par amount outstanding with at least one year to final maturity. The **ICE BofAML US High Yield Index** tracks the performance of U.S. dollar denominated below-investment-grade corporate debt publicly issued in the U.S. domestic market. The **Bloomberg Barclays U.S. Municipal Index** covers the USD-denominated long-term tax exempt bond market (state and local general obligation bonds, revenue bonds, insured bonds and prefunded bonds). The indexes are unmanaged, their returns do not reflect any fees, expenses, or sales charges, and they are not available for direct investment.

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