

## Small-Mid Cap Core Portfolio

Second Quarter 2020 | Managed Accounts



### Portfolio Highlights

**Style:** Small-Mid Cap  
**Sub-Style:** Core  
**Index:** Russell 2500™  
**Portfolio Inception:** 1992  
**Portfolio Assets:** \$6,196.0 M  
**Portfolio Turnover:** 25%–35%

### Portfolio Review

The Small-Mid Cap Core portfolio outperformed the Russell 2500 Index in the second quarter. Performance primarily was driven by an overweight and strong stock selection in the technology and consumer discretionary sectors. Poor stock selection in health care and an underweight in energy detracted from performance.

The biggest contributors to performance during the quarter were DocuSign and Thor Industries.

- As expected, DocuSign reported very strong demand for its core e-signature solutions. These solutions have allowed many businesses to continue working remotely and still be able to execute contracts.
- Due to COVID-19 and its impact on consumers' lack of interest in utilizing airplanes and hotels for travel purposes, the RV industry has experienced healthy demand for Thor's products as traveling in an RV can permit physical distancing and personal living space.
- Other top contributors included Teradyne, Scotts Miracle-Gro and SiteOne Landscape Supply.

The biggest detractors from the portfolio were AMN Healthcare Services and Bright Horizons Family Solutions.

- AMN's business was negatively impacted by COVID-19. As expected, travel nurse demand was particularly high to address COVID cases in hospitals. Elective procedures ground to a halt and with it, demand for other AMN positions declined dramatically.
- Due to the COVID-19 pandemic, Bright Horizons has closed over 75% of its care centers globally that has resulted in a contracted revenue base under its current operating conditions. However, we believe high-quality childcare will continue to be necessary going forward.
- Other detractors included Elanco Animal Health, Interactive Brokers Group and Exponent.

### Purchases and Sales

During the quarter, we purchased Bright Horizons Family Solutions and we sold Winmark.

- Bright Horizons is a primary childcare and back-up care provider that has built a high-quality brand associated with caring for the most precious member of one's family. The business's target market is employer organizations who provide childcare as part of their benefit packages to employees. The business has high switching costs as an employer subsidized childcare program is difficult to transition to another provider.
- We sold Winmark as current operating conditions driven by the COVID-19 pandemic remain highly challenging with mandated store closures and low visibility in terms of both the duration and scale of the impact.

### Outlook

Although the market has greatly recovered this quarter, we do not believe it is anticipating a robust economic recovery as many market commentators have suggested. If businesses were to get back to normal quickly, then many of the hardest hit areas in the stock market would not be 40% to 80% off of their 52-week highs set over the last year when the economy was not in a recession.

Additionally, with the 10-year yield at a paltry 0.65% and the yield curve with only a slightly positive slope, this suggests a modest but not robust recovery. While there continues to be above-average uncertainty (second wave risk, election results, and economic recovery timeline) in the near term, we continue to believe our time-tested strategy of owning quality companies will continue to be rewarded over the long haul.

### Investment Management Team

Name	Years of research experience
<b>Douglas S. Foreman, CFA</b> Chief Investment Officer	34
<b>Jon Christensen, CFA</b> Portfolio Manager + Senior Research Analyst	25
<b>Julie Kutasov</b> Portfolio Manager + Senior Research Analyst	19
<b>Craig Stone</b> Portfolio Manager + Senior Research Analyst	31
<b>Todd Beiley, CFA</b> Senior Research Analyst	21
<b>Julie Biel, CFA</b> Senior Research Analyst	12
<b>Chris Wright, CFA</b> Senior Research Analyst	8
<b>Sean Dixon</b> Research Analyst	11
<b>Adam Xiao, CFA</b> Research Analyst	5
<b>Jordan Greenhouse</b> Senior Portfolio Specialist	23†
<b>James B. May, CFA</b> Portfolio Specialist	32†

### Top Five Holdings

As of June 30, 2020

Company	Percent of equity (%)
DocuSign	7.4
Scotts Miracle-Gro	6.0
Teradyne	5.3
MSCI	4.9
Thor Industries	4.9
<b>Total</b>	<b>28.4</b>

*†Represents years of industry experience.*

*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 be not considered a recommendation or solicitation to purchase securities. A complete listing of portfolio holdings and specific security transactions for the preceding 12 months is available upon request. Holdings are subject to change. Holdings and weightings are based on a representative portfolio. Individual Investors' holdings may differ slightly. Data is obtained by FactSet Research Systems and is assumed to be reliable. Numbers may not always add up due to rounding. Past performance is no guarantee of future results.*

## Investment Process: Discovering Quality

<b>Development of High-Quality Universe</b>	<b>Proprietary Fundamental Research</b>	<b>Portfolio Construction</b>	<b>Sell Discipline</b>
<b>Quantitative Screens</b> <ul style="list-style-type: none"> <li>High return on capital over a full economic cycle</li> <li>Long and resilient earnings history</li> <li>High return on net operating assets</li> <li>Minimal debt</li> </ul> <b>Other Resources</b> <ul style="list-style-type: none"> <li>Research on existing portfolio holdings</li> <li>Meetings with companies</li> <li>Industry reviews</li> <li>Investment conferences</li> <li>Third-party research</li> </ul>	<b>Qualitative Analysis</b> <ul style="list-style-type: none"> <li>Evaluate sustainability of business model and assess management's ability to direct capital where it can create further control of its market</li> </ul> <b>Financial Analysis</b> <ul style="list-style-type: none"> <li>Evaluate basis for superior profitability, long-term growth potential, and ability to allocate capital appropriately</li> </ul> <b>Valuation Analysis</b> <ul style="list-style-type: none"> <li>Determine the current and potential value of the business</li> </ul>	<b>Position Weights</b> <ul style="list-style-type: none"> <li>Maximum initial position size is 5% (at cost)</li> <li>Maximum position size is 10% (at market)</li> </ul> <b>Sector Tolerances</b> <ul style="list-style-type: none"> <li>Seek broad diversification, but no sector constraints</li> </ul> <b>Non-U.S. Holdings</b> <ul style="list-style-type: none"> <li>Up to 20%</li> </ul> <b>Holding Period</b> <ul style="list-style-type: none"> <li>Typically 3-to-5 years, but is often longer</li> <li>Portfolio turnover is typically 25% to 35%</li> </ul> <b>Cash Levels</b> <ul style="list-style-type: none"> <li>Typically will not exceed 10% once a portfolio is fully invested; review by CIO triggered if over 10%</li> </ul>	<b>Extended Valuation</b> <b>Portfolio Upgrade</b> <b>Acquisition Activity</b> <b>Negative Company or Industry Changes</b>

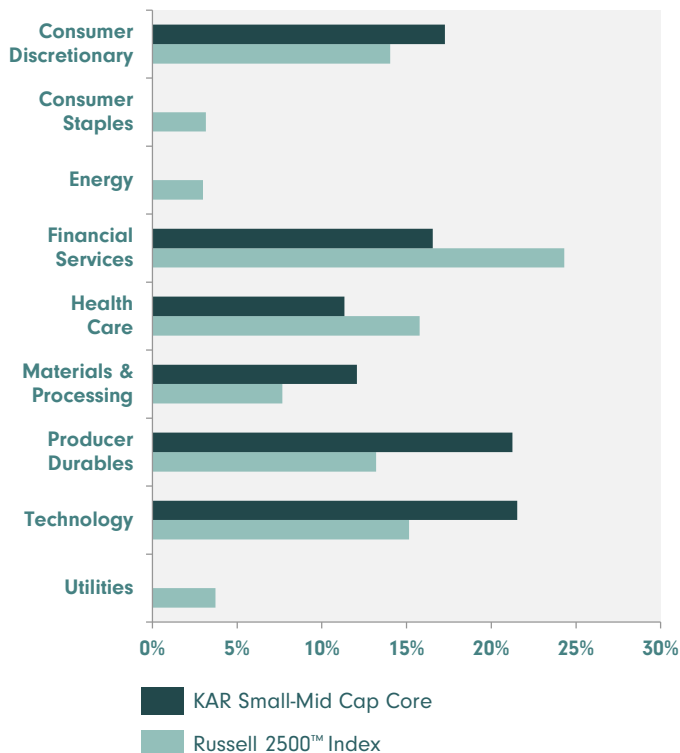
Higher Quality

Stronger, More Consistent Growth

Better Value

## Sector Diversification

As of June 30, 2020



A complete listing of portfolio holdings and specific security transactions for the preceding 12 months is available upon request. Holdings are subject to change. Holdings and weightings are based on a representative portfolio. Individual Investors' holdings may differ slightly. The sector information represented above is based on Russell sector classifications. Data is obtained by FactSet Research Systems and is assumed to be reliable.

## Portfolio Characteristics

As of June 30, 2020

	KAR Small-Mid Cap Core	Russell 2500™ Index
<b>Quality</b>		
Return on Equity—Past 5 Years	22.9%	10.8%
Total Debt/EBITDA	2.3 x	12.0 x
Earnings Variability—Past 10 Years	38.4%	64.7%
<b>Growth</b>		
Earnings Per Share Growth—Past 5 Years	15.7%	9.2%
Earnings Per Share Growth—Past 10 Years	13.8%	9.0%
Capital Generation—{ROE x (1-Payout)}	18.0%	8.0%
<b>Value</b>		
P/E Ratio—Trailing 12 Months	35.4 x	42.6 x
Dividend Yield	0.7%	1.5%
Free Cash Flow Yield†	3.1%	3.7%
<b>Market Characteristics</b>		
\$ Weighted Average Market Cap—3-Year Avg.	\$8.9 B	\$5.1 B
Largest Market Cap—3-Year Avg.	\$19.2 B	\$21.0 B
Annualized Standard Deviation—Since Inception*	16.1%	19.9%

†Free cash flow data is as of March 31, 2020. Prices are as of June 30, 2020. Excludes financials.

\*April 1, 1992

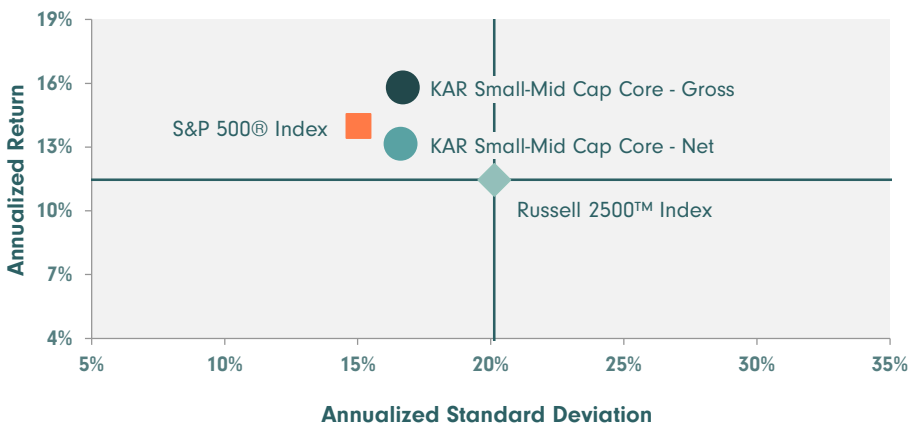
This material is deemed supplemental and complements the performance and disclosure at the end of this presentation. Data is obtained from FactSet Research Systems and BNY Mellon and is assumed to be reliable. Other principal consultant firms may use different algorithms to calculate selected statistics. Estimates are based on certain assumptions and historical information. **Past performance is no guarantee of future results.**

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## Strong Risk-Adjusted Returns

Ten Years Ending June 30, 2020



## Historical Returns

	KAR Small-Mid Cap Core (gross)	KAR Small-Mid Cap Core (net) <sup>†</sup>	Russell 2500™ Index
<b>Annualized Returns (%)<sup>†</sup></b>			
As of June 30, 2020			
2 <sup>nd</sup> Quarter	29.95	29.05	26.56
Year to Date	8.02	6.42	(11.05)
One Year	19.99	16.48	(4.70)
Three Years	17.14	13.71	4.08
Five Years	14.80	11.60	5.41
Seven Years	15.66	12.81	8.15
Ten Years	15.82	13.16	11.46
Inception*	11.74	8.90	9.97
<b>Annual Returns (%)</b>			
2019	40.90	36.84	27.77
2018	(5.23)	(8.05)	(10.00)
2017	19.77	16.28	16.81
2016	17.03	13.61	17.59
2015	5.76	4.10	(2.90)
2014	9.25	7.37	7.07
2013	31.04	29.07	36.80
2012	9.25	7.55	17.88
2011	8.43	6.02	(2.51)
2010	20.23	17.70	26.71
2009	31.12	28.86	34.39
2008	(29.90)	(31.33)	(36.79)
2007	0.26	(1.37)	1.38
2006	14.04	11.75	16.17
2005	3.24	0.14	8.11
2004	13.69	10.26	18.29
2003	25.54	21.91	45.51
2002	(17.31)	(19.84)	(17.80)
2001	4.57	1.53	1.22
2000	23.47	19.85	4.27
1999	7.02	3.93	24.14
1998	20.98	17.42	0.38
1997	21.00	17.45	24.36
1996	26.98	23.22	19.03
1995	18.57	15.07	31.70
1994	2.75	(0.26)	(1.05)
1993	20.00	16.54	16.55
1992 <sup>§</sup>	9.65	7.25	11.36

\*April 1, 1992

<sup>†</sup>All periods less than one year are total returns and are not annualized. Returns are preliminary.

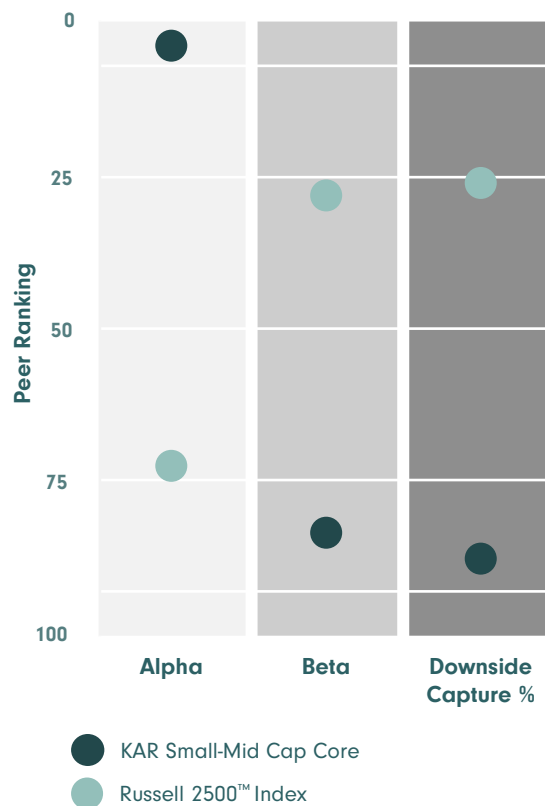
<sup>‡</sup>Net of all fees and expenses. Assumes a 3% annual fee.

<sup>§</sup>Performance calculations are for the nine months ended December 31, 1992.

This material is deemed supplemental and complements the performance and disclosure at the end of this presentation. Returns of the Kayne Anderson Rudnick composite are preliminary and gross of fees unless otherwise specified. For further details on the composite, please see the disclosure statement in this presentation. The Small-Mid Cap Core Universe includes all managers categorized in the small-mid cap core asset class by eVestment. Data is obtained from FactSet Research Systems and is assumed to be reliable. **Past performance is no guarantee of future results.**

## Peer Chart

Ten Years Ending June 30, 2020



## Performance Statistics

Ten Years Ending June 30, 2020

	KAR Small-Mid Cap Core	Russell 2500™ Index
Annualized Return	15.82	11.46
Annualized Standard Deviation	16.69	20.13
Alpha	6.06	0.00
Beta	0.78	1.00
Sharpe Ratio	0.92	0.55
R-Squared	88.81	100.00

**IMPORTANT RISK CONSIDERATIONS: Equity Securities:** The market price of equity securities may be adversely affected by financial market, industry, or issuer specific events. Focus on a particular style or on small or medium-sized companies may enhance that risk. **Limited Number of Investments:** Because the fund has a limited number of securities, it may be more susceptible to factors adversely affecting its securities than a less concentrated fund. **Industry/Sector Concentration:** A fund that focuses its investments in a particular industry or sector will be more sensitive to conditions that affect that industry or sector than a non-concentrated fund.

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### Disclosure

Kayne Anderson Rudnick Investment Management, LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. Kayne Anderson Rudnick Investment Management, LLC has been independently verified for the period from January 1, 1999 through December 31, 2018.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. The Small-Mid Cap Core Wrap Composite has been examined for the period from January 1, 1999 through December 31, 2018. The verification and performance examination reports are available upon request.

Kayne Anderson Rudnick Investment Management, LLC, a wholly owned subsidiary of Virtus Investment Partners, Inc., is a registered investment advisor under the Investment Advisers Act of 1940. Registration of an Investment Advisor does not imply any level of skill or training. Kayne Anderson Rudnick Investment Management, LLC manages a variety of equity and fixed-income strategies focusing exclusively on securities the firm defines as high quality.

The composite includes all fully discretionary Small-Mid Cap Core Wrap Portfolios. Small-Mid Cap Core Wrap Portfolios are invested in equity securities with market capitalizations consistent with the Russell 2500™ Index, that have market control, rising free cash flow, shareholder-oriented management, strong consistent profit growth and low-debt balance sheets. For

comparison purposes, the composite is measured against the Russell 2500™ Index. The Russell 2500™ Index is a market capitalization-weighted index of the 2,500 smallest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. The index is calculated on a total-return basis with dividends reinvested. Benchmark returns are not covered by the report of the independent verifiers. The composite was created in July 2000. A list of composite descriptions and policies for valuing portfolios, calculating performance and preparing compliant presentations are available upon request.

Beginning on January 1, 2006, sub-advisory wrap fee portfolios are also included in composite results. Each sub-advisory relationship is included in the composite as one account. Prior to January 1, 2011, accounts that experienced a significant cash flow, defined as aggregate flows that exceeded 25% of the account's beginning of period market value, were temporarily removed from the composite. Prior to January 1, 2011, the composite minimum was \$100,000.

The standard wrap fee schedule in effect is 3.00% on total assets. Actual management fees charged may vary depending on applicable fee schedules and portfolio size, among other things. Additional information may be found in Part IIA of Form ADV, which is available on request. The performance information is supplied for reference. Past performance is no guarantee of future results. Results will vary among accounts. The U.S. dollar is the currency used to express performance. Performance results include the reinvestment of all income. Prior to December 31, 2005, net annual returns are calculated by deducting 1/4th of an assumed maximum annual wrap fee of 3% from the gross returns on a quarterly basis. Beginning January 1, 2006,

net annual returns are calculated using actual fees incurred. If no fee data is provided by wrap sponsors, the maximum annual wrap fee of 3% is used to calculate net of fee performance. Beginning January 1, 2016, net annual returns are calculated by deducting 1/12th of an assumed maximum annual wrap fee of 3% on a monthly basis. Wrap fees include all charges for trading costs, portfolio management, custody and other administrative expenses.

Internal dispersion is calculated using the asset-weighted standard deviation of annual gross returns for accounts in the composite for the entire year. For those years when less than five accounts were included for the full year, no dispersion measure is presented. The three-year annualized ex-post standard deviation of the composite is presented starting December 31, 2012 because prior to January 1, 2010, the composite return was calculated quarterly and 36 monthly returns are not available.

#### 3-Yr Annualized Standard Deviation (%)

December 31	Composite	Benchmark
2012	15.22	19.24
2013	12.17	15.85
2014	10.13	11.84
2015	12.17	12.59
2016	12.62	13.86
2017	11.16	12.31
2018	13.27	14.30

Year	Total Firm Assets (\$ millions)	Total Composite Assets (\$ millions)	Wrap Accounts as % of Composite Assets	Accounts at Year End	Pure Gross Annual Return (%)*	Net Annual Return (%)	Russell 2500™ Index Annual Return (%)	Internal Dispersion
2009	4,010	342	100%	64	31.12	28.86	34.39	0.64
2010	4,729	316	100%	59	20.23	17.70	26.71	0.35
2011	5,232	337	100%	53	8.43	6.02	(2.51)	0.78
2012	6,545	422	100%	44	9.25	7.55	17.88	0.62
2013	7,841	362	100%	39	31.04	29.07	36.80	0.36
2014	7,989	373	100%	35	9.25	7.37	7.07	0.16
2015	8,095	378	100%	30	5.76	4.10	(2.90)	0.19
2016	9,989	369	100%	30	17.03	13.61	17.59	0.38
2017	14,609	518	100%	32	19.77	16.28	16.81	0.26
2018	17,840	618	100%	24	(5.23)	(8.05)	(10.00)	0.17

\*Pure gross returns are supplemental to net returns.

The Russell 2500™ Index is a trademark/service mark of Frank Russell Company. Russell® is a trademark of Frank Russell Company.