



Market Commentary

Value Equity Strategies



Second Quarter 2025

Second Quarter Sentiment Shift

The second quarter was quite the contrast to the first as investor sentiment grew wildly optimistic throughout the quarter after a rather dour start to the year. We entered the year with a lot of anxiety surrounding the economic agenda of the new administration, whose focus was primarily on restructuring the global order in an attempt to stem the widening trade imbalances that have benefited capital holders at the expense of labor. The administration's preferred policy approach, which had been widely communicated, was through tariffs; in early April, they released the initial tariff framework. It was more abrupt and disruptive than investors expected, and the markets responded accordingly, pushing the broad equity markets into a sharp correction during the first part of April. It was not until signals (tweets, to be precise) reflected a softer stance in tariff negotiations that the markets turned, and a strong rally ensued through quarter-end.

Market Rotation

In light of these developments, it has truly been a tale of two markets. The broad markets sold off through early April, with the S&P 500 Index down roughly 15% by April 8, before staging a ~25% rally, resulting in a year-to-date return of 6.0%. The underlying drivers of performance were also quite different, leading to a rotation in leadership. During the first part of the year, the market was led by defensive areas such as Consumer Staples, Health Care, and Utilities as well as Energy. These sectors are weighted much heavier in the Value indexes and provide higher dividend yields, which caused value to outperform growth. The rotation that occurred in the second quarter spread across indexes, styles, sectors, factors, and the Magnificent 7 (see Figure 1). The graph illustrates investors' rapid shift to risk, with momentum and higher beta (risk) factors leading the market in the second quarter.

Figure 1

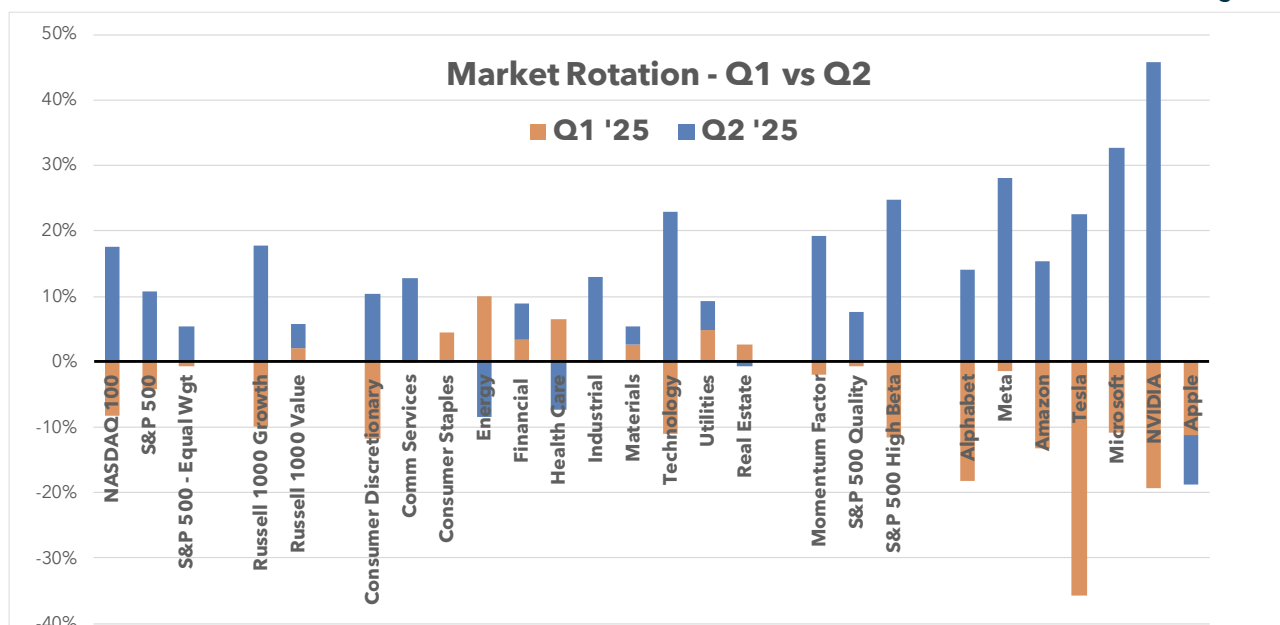
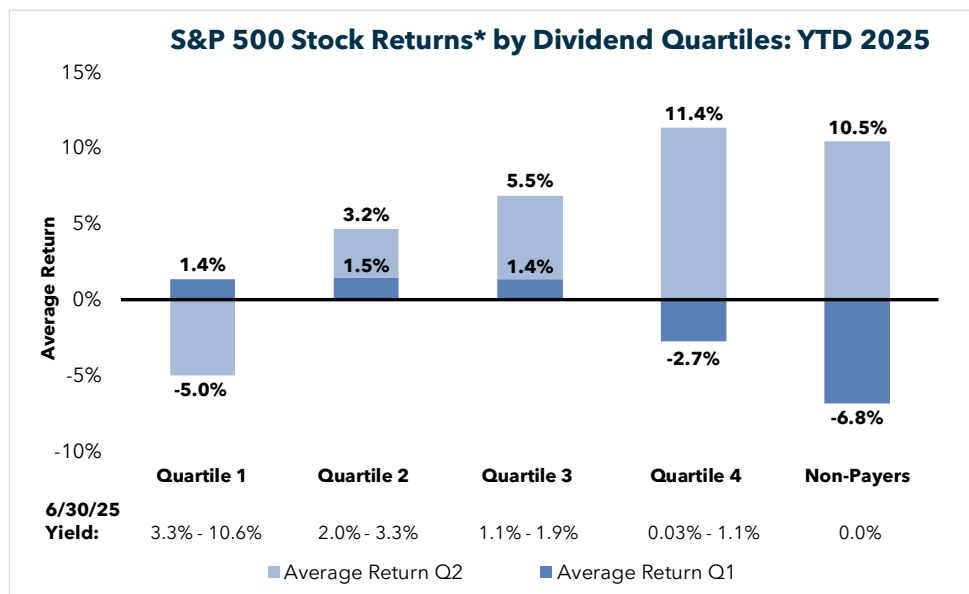


Figure 1: Sources: NASDAQ-100 Index (NDX), SPDR S&P 500 ETF Trust (SPY), Invesco S&P 500 Equal Weight ETF (RSP), iShares Russell 1000 Growth ETF (IWF), iShares Russell 1000 Value ETF (IWD), Consumer Discretionary Select Sector SPDR Fund (XLY), Communication Services Select Sector SPDR Fund (XLC), Consumer Staples Select Sector SPDR Fund (XLP), Energy Select Sector SPDR Fund (XLE), Financial Select Sector SPDR Fund (XLF), Health Care Select Sector SPDR Fund (XLV), Industrial Select Sector SPDR Fund (XLI), Materials Select Sector SPDR Fund (XLB), Technology Select Sector SPDR Fund (XLK), Utilities Select Sector SPDR Fund (XLU), Vanguard Real Estate ETF (VNQ), iShares MSCI USA Momentum Factor ETF (MTUM), Invesco S&P 500 Quality ETF (SPHQ), Invesco S&P 500 High Beta ETF (SPHB), Alphabet Inc. Class A (GOOGL), Meta Platforms Inc. Class A (META), Amazon.com, Inc. (AMZN), Tesla, Inc. (TSLA), Microsoft Corporation (MSFT), NVIDIA Corporation (NVDA), and Apple Inc. (AAPL)

Impact on Dividend-Paying Stocks

The rotation toward momentum/risk in the second quarter was also evident for dividend investors. The non-payers and low-dividend payers were down in the first quarter, while businesses with dividend yields higher than 1.1% posted positive returns on average. Conversely, in the second quarter, the non- and low-dividend payers posted low double-digit returns, while the higher yield quartiles lagged, with the highest-paying quartile posting a loss. Figure 2 illustrates the quarter-over-quarter performance differentials by yield quartile.

Figure 2



*Actual Historical Constituents. Returns through 6/30/2025.
(Sources: Confluence, Ned Davis Research)

This also marks the third rotation since last summer. If you recall, the mega-cap, tech-oriented Magnificent 7 ceded leadership during the summer of 2024, briefly retaking the role later in 2024. This back-and-forth is common after extended periods of relative outperformance as investors are often hesitant to abandon strategies that have been working. It is also a reflection of the underlying economic backdrop that fueled the rise in populism and the current administration's efforts to address these conditions, which will continue to impact the markets.

We examined this influence on the markets in our recent *Value Equity Insights* publication, "[Investing Where the Puck is Going: The Renewed Case for Active and Value.](#)"

Market Outlook

Looking forward, we anticipate heightened volatility as the administration is attempting to pull levers that have not been used in this manner for many generations and are likely to produce varying responses and secondary effects. Fortunately, the economy remains on decent footing and the recently passed budget reconciliation law provides clarity for businesses and taxpayers. This bodes well for the outlook on the economy and earnings. As always, we believe long-term investors should view volatility as an opportunity – a principle central to our investment philosophy.

Confluence Value Equities Investment Committee

Mark Keller, CFA	Tore Stole	Tom Dugan, CFA	Dustin Hausladen	Brett Mawhiney, CFA	John Koenig, CFA
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Select Equity Income

Value Equity Strategies



Second Quarter 2025

Select Equity Income invests in large capitalization businesses that collectively generate an above-average stream of dividend income, while also providing capital appreciation potential. The businesses are selected using a bottom-up, fundamental research process that seeks to identify individual businesses that have the ability to either pay a high level of dividend income or grow the dividend stream over time. The strategy is appropriate for clients seeking total return from dividend income and capital appreciation.

Strategy Commentary

The objective of the Confluence Select Equity Income strategy is to provide an above-average stream of income balanced with capital appreciation, while delivering reasonable dividend growth to protect purchasing power. The strategy accomplishes this by investing in companies with durable competitive advantages and ample cash flow. These companies are typically mature, well-capitalized, and in a strong position to return cash to shareholders through dividend payments and share repurchases.

This focus on quality businesses with favorable current dividends has been shown to provide a measure of ballast in difficult markets as cash flow is returned to shareholders in the near term (dividends), unlike younger or faster-growing businesses, which typically need that capital to maintain their growth. The shorter-duration, higher-yielding businesses also tend to trade at lower valuations, which can provide downside protection when sentiment shifts.

Despite the relative volatility of the market year-to-date, Select Equity Income has continued to return consistent (and growing) dividend income. As stated in the table (Figure 1), 13 of the 25 companies in the current Select Equity Income portfolio have increased their dividends, with an average announced growth rate of 4.0%. As of June 30, 2025, the average dividend yield for the Select Equity Income portfolio is 3.3% (source: FactSet).

Figure 1 – Annual Dividend Statistics for Select Equity Income Portfolio at 12/31 (Dividend Growth Using Announcement Date)¹

Year	Holdings	Avg. Yield ⁺	Dividend Change from Prior Year**			Avg. Growth***
			# of companies with			
			Increase	Flat	Decrease	
2020*	24	3.2%	18	6	0	5.2%
2021	24	2.7%	21	3	0	5.9%
2022	24	3.1%	22	2	0	6.1%
2023	26	3.2%	21	5	0	5.1%
2024	25	3.2%	22	3	0	5.0%
Average-5 yrs (2020-2024)		3.1%	21	4	0	5.5%
As of 6/30/2025	25	3.3%	13		0	4.0%

* 2020 excludes impact of temporary dividend suspensions during the pandemic of 2020. ** Dividend Change from Prior Year excludes impact of special dividends and spin-offs.

*** For monthly/YTD data, the average growth rate is calculated using only those holdings for which an increase or decrease in the indicated annual dividend amount has been announced.

Full-year statistics are calculated as the average of all holdings, including those which did not announce a change to their indicated annual dividend during the year.

+ Avg. Yield column is the equal-weighted average dividend yield of portfolio holdings at 12/31, calculated based on annualized current dividend plus any special dividend paid during the year.

Avg. Yield as of 6/30/2025 calculated using Indicated Annual Dividend (IAD) from FactSet.

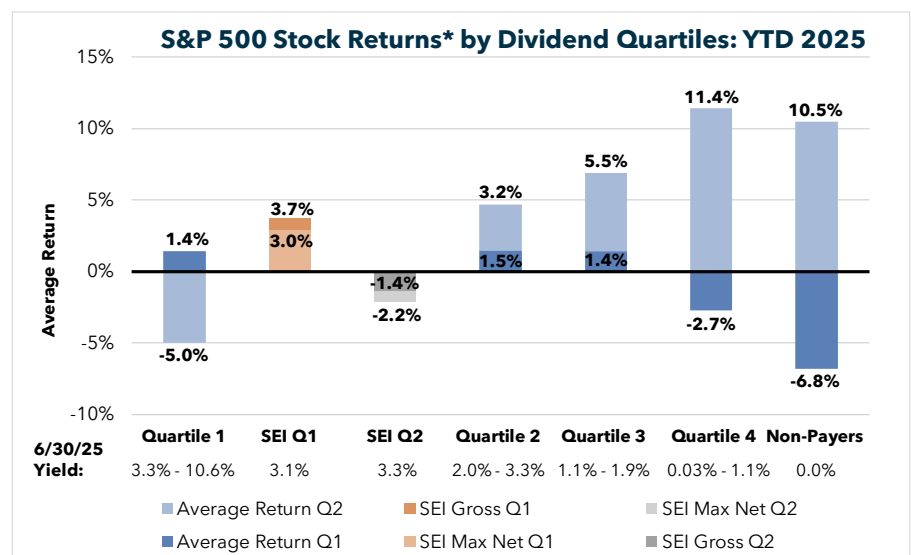
As discussed in the Market Commentary, the indexes have more than recovered their early losses this year, with the S&P 500 Index now up 6.2% year-to-date compared to -4.3% in the first quarter. Continued geopolitical and economic uncertainty over the course of the year has led to multiple shifts in the market's risk appetite, starting with a strong movement toward lower-risk, value, and yield-oriented stocks in the first quarter that sharply reverted to riskier growth and momentum stocks during the second quarter. The Information Technology sector of the S&P 500 rose 8.1% year-to-date, significantly recovering from a first quarter return of -12.7%. Communication Services rebounded similarly, delivering an 11.1% return year-to-date after a first quarter return of -6.2%. The Magnificent 7 stocks are represented heavily in both of these sectors and contributed to their strong performance, while the traditionally higher yielding, less cyclical sectors like Utilities, Health Care, and Consumer Staples lagged behind.

Strategy Commentary continued...

Consumer Staples performance within the S&P 500 was particularly bifurcated; in fact, the sector's entire positive return for the year was driven by the top five performers, highlighting the overall weakness of the sector outside of those stocks. Among those top five contributors, half of the return was generated by tobacco companies. Producers and manufacturers of food, beverage, and household goods generally underperformed. In response to a stretched and cautious consumer, the largest distributors have been exerting pressure on food and packaged goods producers, maintaining or even reducing retail prices despite continued input cost inflation. Against this backdrop, Walmart and Costco, already trading at or near record-high valuations, continued to outperform the rest of the Consumer Staples sector and were among the top five contributors for the sector as well.

Market participants also showed a sharp reversal in their appetite for yield, most notably at the highest and lowest yield levels. Stocks with dividend yields in the top quartile have underperformed year-to-date despite strongly outperforming the bottom quartile and non-payers in the first quarter. Though stocks in the second and third quartile performed better, they were still noticeably outpaced by the lowest yielders.

This chart (Figure 2), based on data from Ned Davis Research, illustrates the quarter-over-quarter performance of S&P 500 returns segmented by dividend yield quartile. We have positioned Select Equity Income on the chart where it falls in terms of yield, between Quartiles 1 and 2, and we see a similar rotation when comparing its Q1 (orange) and Q2 (gray) performance returns.



*Actual Historical Constituents. IAD strategy yield and returns as of 6/30/2025. (Sources: Confluence, Ned Davis Research, FactSet)

For patient investors with a long-term perspective, this dislocation can provide opportunities to own high-quality companies that generate strong, consistent, and growing dividend income streams at attractive valuations. In the meantime, the market dynamics previously discussed contributed to Select Equity Income's underperformance year-to-date, returning 2.2% (gross of fees) compared to the 6.2% return of the S&P 500. [The strategy's net-of-fees return for the same period was 0.7% YTD. See disclosures on last page for fee description; actual investment advisory fees may vary.]

Year-to-date performance in the Select Equity Income strategy was led by Northern Trust Corp. (NTRS), Gilead Sciences (GILD), and Cisco Systems (CSCO).

Northern Trust was supported by unconfirmed reports that BNY Mellon had approached the bank about a merger, potentially combining two of the world's largest asset management firms. Gilead continues to experience success with its pipeline and the market is beginning to adjust expectations. Cisco Systems saw higher demand for its core routing and switching products, bolstered by increased demand within the AI end market, while its acquisition of Splunk last year has delivered strong results.

The laggards for the quarter were Dow Inc. (DOW), Clorox Co. (CLX), and Diageo (DEO).

Dow has been pressured by increased concern in the market over the company's tariff exposure and export-related demand, particularly around ethylene and polyethylene products of which the company is the #1 global producer. Clorox has experienced headwinds from continued inflation as consumers have tightened their wallets and retailers such as Walmart and Costco have exerted pressure on food, beverage, and household goods producers to absorb inflation-related costs. Finally, Diageo's portfolio of global spirits and alcoholic beverages portfolio has been impacted by uncertainty around tariff policy combined with inflation-driven reductions in consumer spending. Data so far indicates the bulk of these issues are shorter-term and cyclical, and we believe Diageo's strong portfolio of premium brands should align well with long-term trends toward higher-value beverages going forward.

Outlook

Though markets appear to have mostly recovered from the initial waves of uncertainty introduced by shifts in US trade policy earlier this year and the potential for renewed inflationary headwinds, these challenges are far from resolved. While companies, consumers, and markets interpret and adjust to these changes, we see potential for periods of further market volatility driven by these issues. Artificial intelligence is also likely to continue garnering significant attention from market participants seeking to identify which companies will be winners and losers in the rapidly evolving technology landscape.

We remain rooted in our focus on finding competitively advantaged, highly cash generative companies led by management teams with a proven track record of successful capital allocation. Companies with these attributes are well positioned to protect and maintain their business during periods of uncertainty, deploy their cash meaningfully when market valuations provide M&A and share repurchase opportunities, and rapidly invest capital to grow sales and market share when short-term headwinds abate.

We continue to emphasize the importance of dividend-paying stocks that can maintain high (and even growing) dividends, providing ballast during periods of market instability. While these stocks may move in and out of favor with markets, we remain focused on the fundamental aspects of the underlying businesses that should ultimately provide reliable income streams for our clients and protect purchasing power over the long-term.

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Contribution²

The top contributors and detractors for the portfolio in Q2 2025 and the full year are shown in the following tables:

(QTD as of 6/30/2025)

Security	Avg Weight (%)	Contribution (%)
Top 5		
Northern Trust Corp.	4.37	1.24
Analog Devices Inc.	4.34	0.81
Cisco Systems Inc.	3.95	0.53
US Bancorp	4.05	0.36
Kinder Morgan Inc.	4.20	0.18
Bottom 5		
Chevron Corp.	2.84	(0.45)
PepsiCo Inc.	3.76	(0.46)
Clorox Co.	3.28	(0.64)
Fidelity National Financial Inc.	5.32	(0.76)
Dow Inc.	3.03	(0.79)

(YTD as of 6/30/2025)

Security	Avg Weight (%)	Contribution (%)
Top 5		
Northern Trust Corp.	4.39	1.15
Gilead Sciences Inc.	4.22	0.78
Cisco Systems Inc.	3.90	0.73
Progressive Corp.	4.44	0.69
Analog Devices Inc.	4.00	0.67
Bottom 5		
PepsiCo Inc.	3.15	(0.46)
United Parcel Service Inc.	3.13	(0.58)
Diageo plc	3.70	(0.76)
Clorox Co.	3.47	(0.99)
Dow Inc.	2.67	(1.08)

Performance Composite Returns³ (For Periods Ending June 30, 2025)

	Since Inception**	5-Year*	3-Year*	1-Year	YTD	QTD
Select Equity Income						
Pure Gross-of-Fees ⁴	13.7%	13.7%	12.7%	17.4%	2.2%	(1.4%)
Max Net-of-Fees ⁵	10.3%	10.3%	9.4%	13.9%	0.7%	(2.2%)
Russell 1000 Value	13.9%	13.9%	12.7%	13.7%	6.0%	3.8%
S&P 500	16.6%	16.6%	19.7%	15.1%	6.2%	10.9%

Calendar Year	Pure Gross-of-Fees ⁴	Max Net-of-Fees ⁵	R1000 Value	S&P 500	Difference (Gross-R1000V)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	R1000V 3yr Std Dev	S&P 500 3yr Std Dev	Composite Dispersion
2020**	15.4%	13.7%	22.7%	22.2%	(7.4%)	1	\$116	\$6,889,798	N/A	N/A	N/A	N/A
2021	28.0%	24.2%	25.1%	28.7%	2.9%	1	\$148	\$7,761,687	N/A	N/A	N/A	N/A
2022	(2.4%)	(5.3%)	(7.6%)	(18.1%)	5.2%	1	\$145	\$6,931,635	N/A	N/A	N/A	N/A
2023	9.5%	6.3%	11.4%	26.3%	(1.9%)	9	\$3,103	\$7,200,019	15.1%	16.5%	17.3%	N/A
2024	17.5%	14.1%	14.3%	25.0%	3.2%	110	\$44,823	\$7,280,773	14.6%	16.7%	17.2%	0.1%

*Average annualized returns

**Inception is 7/1/2020

See performance disclosures on last page.

Portfolio Benchmarks

Russell 1000[®] Value Index - A capitalization-weighted index designed to measure performance of those Russell 1000[®] Index companies with lower price-to-book ratios and lower forecasted growth values.

S&P 500[®] Index - A capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. (Source: Bloomberg)

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Indexes: The Russell 1000 Value and S&P 500 are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only & do not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.

¹Annual Dividend Statistics—Figure 1: Dividend growth based on when the increase was announced. Annual dividend income history is available upon request. Current portfolio statistics exclude companies that have been sold and include companies that have been purchased year-to-date.

²Contribution—Contribution data shown from a sample account, based on individual stock performance and portfolio weighting. Table showing the top 5 contributors/detractors reflects the strategy's best and worst performers (net), based on each holding's contribution to the sample account for the period stated. Holdings identified do not represent all of the securities purchased, sold or recommended. Individual client portfolios in the strategy may differ, sometimes significantly, from these listings.

³Performance Composite Returns—Confluence 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. Confluence Investment Management LLC has been independently verified for the periods August 1, 2008, through December 31, 2024. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards.

Verification provides assurance on whether the firm's policies and procedures related to composite maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report.

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The Select Equity Income strategy was inceptioned on July 1, 2020, and the current Select Equity Income Composite was created on May 1, 2023. Confluence Investment Management LLC is an independent registered investment adviser. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. The US dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

⁴Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

⁵Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite is as follows: 0.60% on the first \$500,000; 0.55% on the next \$500,000; and 0.50% over \$1,000,000. There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Bundled fee accounts make up 0% of the composite. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Performance prior to May 1, 2023, is based on the Select Equity Income-Direct Composite which was created on July 1, 2020. This composite includes accounts that pursue the Select Equity Income strategy, but have a different fee structure. Gross returns from the Select Equity Income-Direct Composite include transaction costs and net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly.

A complete list of composite descriptions is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. The annual composite dispersion is an equal-weighted standard deviation, using gross-of-fee returns, calculated for the accounts in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Select Equity Income Composite contains fully discretionary Select Equity Income wrap accounts. Select Equity Income is a value-based, bottom-up portfolio that invests in stocks from market capitalizations typically exceeding \$10 billion based on their ability to generate an above-average stream of dividend income, while also providing capital appreciation potential.

****Results shown for the year 2020 represent partial period performance from July 1, 2020, through December 31, 2020. N/A-Composite Dispersion:** Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. N/A-3yr Std Dev: Composite does not have 3 years of monthly performance history.