



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

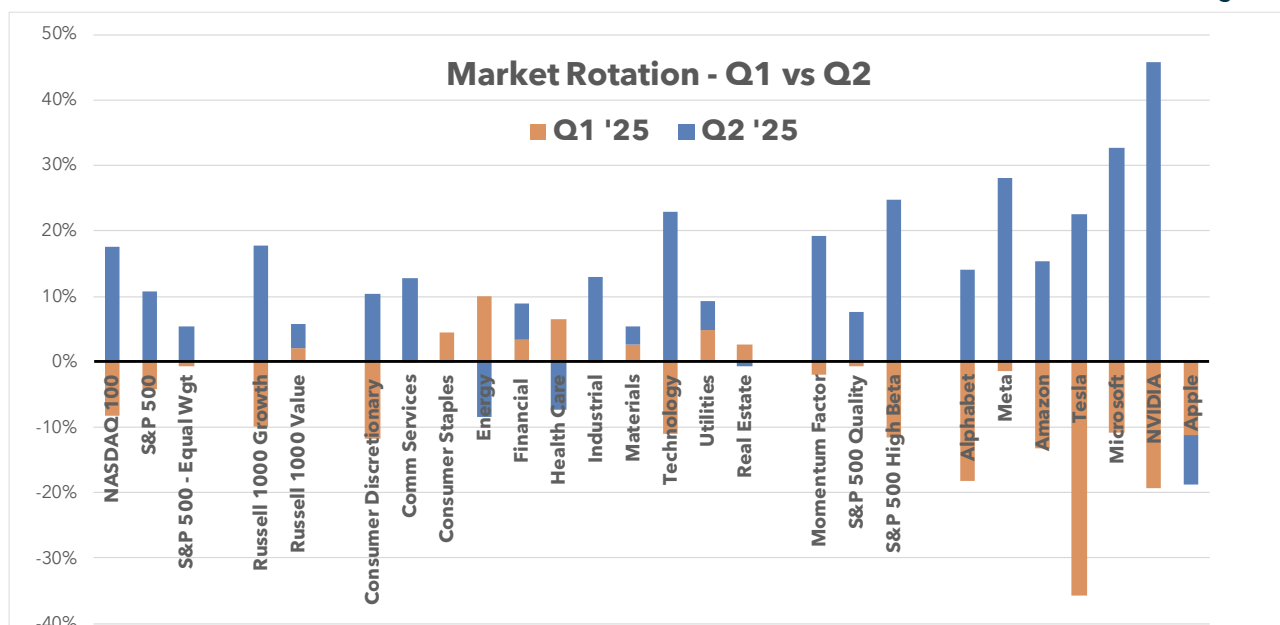
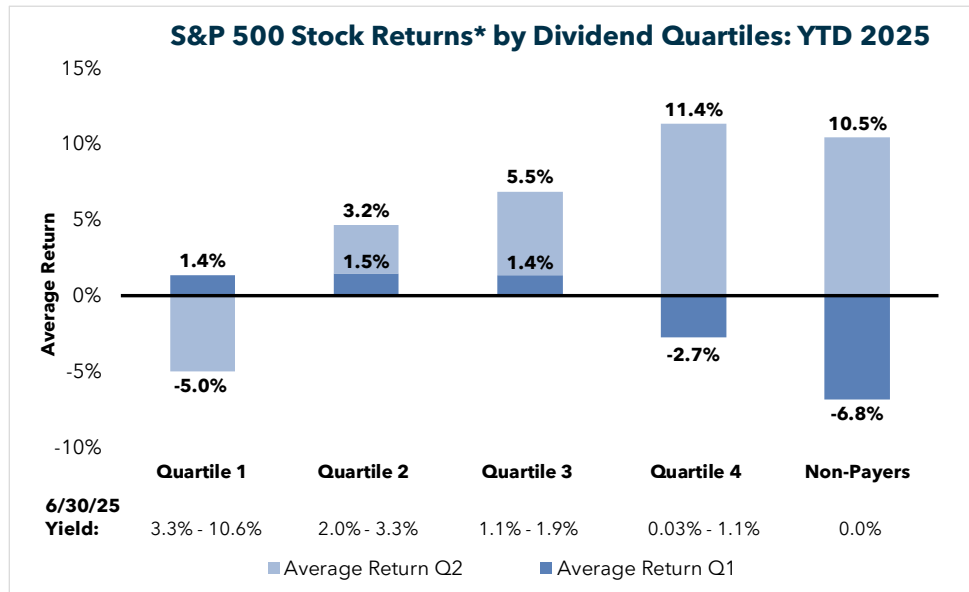


Figure 1: Sources: NASDAQ-100 Index (NDX), SPDR S&P 500 ETF Trust (SPY), Invesco S&P 500 Equal Weight ETF (RSP), iShares Russell 1000 Growth ETF (IWF), iShares Russell 1000 Value ETF (IWD), Consumer Discretionary Select Sector SPDR Fund (XLY), Communication Services Select Sector SPDR Fund (XLC), Consumer 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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Value Opportunities

Value Equity Strategies



Second Quarter 2025

Value Opportunities is a concentrated portfolio of businesses that range in market capitalization. Companies are selected using a bottom-up, fundamental research process that seeks to identify individual businesses that are trading at substantial discounts to our estimate of intrinsic value and have near-term catalysts in which to unlock the value. The portfolio may have concentrations in both individual holdings and/or industries. The portfolio typically comprises 8-12 holdings and is expected to result in high annual turnover. The strategy is appropriate for clients seeking an aggressive approach to generating capital appreciation.

Strategy Commentary

With the S&P 500 Index up 6.2% in the first half of 2025, one could conclude that it's been a fairly typical six months. However, for those of us that lived through it, we know differently as we have dealt with issues such as a global trade war, an onslaught of White House policy changes, and the US bombing of Iran's nuclear facilities, to name a few. This brought a lot of unpredictable market volatility and is a good reminder that there is a big difference between reading about history and living through it – especially as a patient, long-term investor.

As a result, the relative year-to-date performance reported through June looks very different than it did during the April tariff selloff or even just a month prior. Year-to-date, the S&P 500, Russell 3000 Value, and the Confluence Value Opportunities strategy have returned 6.2%, 5.5%, and -0.3% (gross of fees), respectively, but just a month ago, those figures through the end of May were 1.1%, 2.0%, and 0.6%, respectively. For the second quarter overall, the S&P 500 was up 10.9%, outperforming the Russell 3000 Value, up 3.8%, and Value Opportunities, up 2.3% (gross of fees). *[The strategy's net-of-fees returns for the same periods were -1.8% YTD and +1.6% QTD. See disclosures on last page for fee description; actual investment advisory fees may vary.]*

So, what changed in June? The market moved decisively back toward what has led for the past five years – favoring cyclical, mega-cap, growth stocks – and away from defensive, value stocks. But the reasons for the rotation are not entirely clear, given the high level of economic uncertainty from tariffs and interest rates along with weak consumer and business confidence.

With the move toward cyclical, mega-cap, growth stocks, the more defensive and value-focused companies in the Value Opportunities portfolio lagged behind. In particular, almost all of the year-to-date relative underperformance versus the S&P 500 was from Tripadvisor and our Health Care holdings (CONMED and Charles River Laboratories). Additionally, two of our top contributors year-to-date (Progressive and Paycom) were the weakest performers in June due to the market's quick embrace of cyclical mega-cap stocks.

Still, in a concentrated portfolio of quality businesses, things can change quickly. In early July, it was disclosed that activist investor Starboard Value had built a 9% stake in Tripadvisor (TRIP). As a result, the stock was up almost 40% in early July with further upside to the private equity takeout offers the company entertained in 2024. With the catalyst from a simplified ownership structure, it looks like Starboard also sees the opportunity we discussed last quarter when we added Tripadvisor to the portfolio.

CONMED Corp. (CNMD) has also been a weak performer year-to-date (down approximately 23%) and is a great example of just how cheap small cap stocks have become, even ones that are high quality, profitable, and growing. CONMED is a medical technology company that provides mostly single-use devices and equipment for surgical procedures. The company gets many of its product ideas from the surgeons themselves, which creates a very sticky relationship with surgeons who become accustomed to the solutions that CONMED offers.

When we added CONMED to the portfolio last year, the stock was attractively valued, and we believe now it is even more so at only 11x forward earnings. In the current stock market environment, there are many inexpensive small cap stocks that keep getting cheaper as everyone is chasing the mega-cap growth companies. But this won't go on forever. As the famous value investor, Ben Graham, said, "In the short run, the market is a voting machine but in the long run, it is a weighing machine." Just to clarify, over the long term, the market is not weighing for size or market capitalization but rather for intrinsic value. And based on intrinsic value, CONMED is trading at a significant discount in our estimation.

Strategy Commentary continued...

Lastly, Dollar Tree (DLTR) has been our top performer in 2025 (up over 30%), after being the biggest detractor in 2024 (down roughly 47%) as our thesis and catalysts are playing out. With prolonged economic weakness, middle- and upper-income shoppers are starting to trade down to low-priced retail, and management is now fully focused on the Dollar Tree concept after the successful divestiture of Family Dollar earlier this year.

During the second quarter, we sold The Azek Co. (AZEK), which is being acquired by James Hardie Industries, at an exit price of around \$55, on average, in order to buy a new position that is still in progress. Azek is a high-quality business and was a successful investment in the Value Opportunities portfolio, up over 3x from our initial purchase in October 2022 around \$17.

Outlook

It took the S&P 500 only 55 days to rebound from the selloff in April, beating the previous record for the fastest recovery (following a drawdown of at least 15%) set in 1998 during the dot-com speculative mania (*source: Strategas*). The swift turnaround indicates that the market is becoming increasingly confident that a recession can be avoided.

Since the 2008 financial crisis, US monetary and fiscal policy has doused any potential recession fires, but government debt and interest rates are piling up. It is especially difficult to know where the fed funds rate is headed from here, but globalization, record debt issuance, and persistent inflation will likely push long-term interest rates higher, not lower.

In such an environment, defensive, value-oriented stocks are well positioned to outperform, aligning with our investment philosophy and approach. As always, we are long-term investors, so we will continue to focus on buying great companies with capable management teams at a discount to our estimate of intrinsic value.

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Contribution¹

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		
Dollar Tree Inc.	9.68	2.82
Paycom Software Inc.	14.49	0.90
Keysight Technologies Inc.	6.78	0.64
i3 Verticals Inc.	5.34	0.64
Azek Co. Inc.	Sold	0.58
Bottom 5		
Diageo plc	8.20	(0.09)
JBT Marel Corp.	12.15	(0.38)
Progressive Corp.	11.60	(0.66)
TripAdvisor Inc.	8.79	(0.83)
CONMED Corp.	7.33	(1.16)

(YTD as of 6/30/2025)

Security	Avg Weight (%)	Contribution (%)
Top 5		
Dollar Tree Inc.	8.76	2.79
Paycom Software Inc.	13.50	1.71
Progressive Corp.	11.78	1.48
Azek Co. Inc.	Sold	1.00
i3 Verticals Inc.	5.29	0.94
Bottom 5		
JBT Marel Corp.	12.62	(0.72)
Charles River Laboratories International	6.08	(1.45)
Diageo plc	8.26	(1.72)
CONMED Corp.	7.85	(2.15)
TripAdvisor Inc.	8.08	(2.32)

Performance Composite Returns² (For Periods Ending June 30, 2025)

	Since Inception**	25-Year*	20-Year*	15-Year*	10-Year*	5-Year*	3-Year*	1-Year	YTD	QTD
Value Opportunities										
Pure Gross-of-Fees ³	9.9%	10.0%	9.2%	10.7%	5.5%	7.9%	11.1%	4.7%	(0.3%)	2.3%
Max Net-of-Fees ⁴	6.7%	6.9%	6.0%	7.5%	2.4%	4.7%	7.8%	1.6%	(1.8%)	1.6%
S&P 500	7.8%	8.0%	10.7%	14.9%	13.6%	16.6%	19.7%	15.1%	6.2%	10.9%
Russell 3000 Value	7.6%	7.9%	8.0%	11.4%	9.0%	13.8%	12.4%	13.3%	5.5%	3.8%

Calendar Year	Pure Gross-of-Fees ³	Max Net-of-Fees ⁴	S&P 500	R3000 Value	Difference (Gross-S&P500)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	S&P 500 3yr Std Dev	R3000V 3yr Std Dev	Composite Dispersion
2005**	4.4%	1.6%	4.9%	6.9%	(0.5%)	179	\$23,399		11.7%	9.0%	9.7%	0.8%
2006	27.0%	23.6%	15.8%	22.3%	11.3%	171	\$19,132		7.6%	6.8%	7.0%	1.7%
2007	2.1%	(0.7%)	5.5%	(1.0%)	(3.4%)	197	\$20,510		8.4%	7.7%	8.3%	0.7%
2008	(22.3%)	(24.5%)	(37.0%)	(36.2%)	14.7%	29	\$8,299	\$291,644	18.6%	15.1%	15.5%	N/A
2009	31.5%	27.6%	26.5%	19.8%	5.0%	37	\$14,001	\$533,832	25.2%	19.6%	21.3%	2.0%
2010	6.9%	3.7%	15.1%	16.3%	(8.2%)	51	\$7,429	\$751,909	27.9%	21.9%	23.5%	0.7%
2011	(1.7%)	(4.6%)	2.1%	(0.1%)	(3.8%)	53	\$7,694	\$937,487	23.7%	18.7%	21.0%	0.6%
2012	28.5%	24.7%	16.0%	17.6%	12.5%	53	\$9,576	\$1,272,265	18.3%	15.1%	15.8%	0.9%
2013	32.3%	28.3%	32.4%	32.7%	(0.1%)	76	\$18,299	\$1,955,915	13.5%	11.9%	12.9%	0.4%
2014	31.6%	27.7%	13.7%	12.7%	17.9%	110	\$31,040	\$2,589,024	11.4%	9.0%	9.4%	0.9%
2015	2.3%	(0.7%)	1.4%	(4.1%)	1.0%	554	\$113,587	\$3,175,419	10.8%	10.5%	10.7%	0.3%
2016	15.4%	12.0%	12.0%	18.4%	3.4%	959	\$207,565	\$4,413,659	10.9%	10.6%	11.0%	0.5%
2017	14.5%	11.1%	21.8%	13.2%	(7.3%)	1,737	\$359,636	\$5,944,479	9.8%	9.9%	10.3%	0.8%
2018	(18.8%)	(21.2%)	(4.4%)	(8.6%)	(14.4%)	1,494	\$236,097	\$5,486,737	11.9%	10.8%	11.1%	0.8%
2019	28.6%	24.7%	31.5%	26.2%	(2.9%)	1,129	\$230,991	\$7,044,708	13.6%	11.9%	12.0%	0.7%
2020	9.5%	6.2%	18.4%	2.9%	(8.9%)	745	\$165,389	\$6,889,798	20.0%	18.5%	20.0%	1.3%
2021	6.9%	3.8%	28.7%	25.3%	(21.7%)	532	\$132,656	\$7,761,687	18.3%	17.2%	19.3%	1.2%
2022	(22.3%)	(24.6%)	(18.1%)	(8.0%)	(4.1%)	331	\$61,497	\$6,931,635	21.1%	20.9%	21.5%	0.9%
2023	30.6%	26.7%	26.3%	11.6%	4.3%	250	\$61,922	\$7,200,019	19.5%	17.3%	16.7%	0.6%
2024	8.8%	5.6%	25.0%	14.0%	(16.2%)	223	\$61,505	\$7,280,773	21.2%	17.2%	16.9%	1.1%

*Average annualized returns **Inception is 4/1/2000. Additional years of performance available on our website. See performance disclosures on last page.

Portfolio Benchmarks

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.

Russell 3000[®] Value Index – A capitalization-weighted index designed to measure performance of those Russell 3000[®] Index companies with lower price-to-book ratios and lower forecasted growth values. (Source: Bloomberg)

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Indexes: The S&P 500 and Russell 3000 Value 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.

¹Contribution—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.

²Performance 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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³ Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

⁴ Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly (2.75% prior to 7/1/08). This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite is as follows: 1.00% on the first \$500,000; 0.90% on the next \$500,000; and 0.75% 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 100% of the composite for all periods. 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.

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 Value Opportunities Composite contains fully discretionary Value Opportunities wrap accounts. Value Opportunities is a concentrated, value-based, bottom-up portfolio that utilizes stocks from all market capitalizations with a focus on near-term catalysts. Catalysts include reorganizations, turnarounds, and other unique situations that are anticipated to come to fruition in approximately 6-18 months. This short-term investment time frame often leads to high turnover. *Because of the concentrated positions, the portfolio is more susceptible to movements of any one holding.*

****Results shown for the year 2000 represent partial period performance from April 1, 2000, through December 31, 2000. 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.