First Quarter
2016

Equity Strategies • Equity Income

The Equity Income portfolio is focused on businesses across a broad range of market capitalizations that collectively generate an above-average stream of dividend income, while also providing for 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 portfolio typically is comprised of 30-35 holdings and is expected to result in low to moderate turnover. The portfolio is suitable for clients seeking total return from dividend income and capital appreciation.

Portfolio Commentary

The S&P 500 Index rose 1.3% during the first quarter while the Equity Income portfolio gained 7.7% (gross of fees) over the same period. *For detailed performance data and disclosures see: http://www.confluenceinvestment.com/equity_strategies#prod_137*

There are several ways to explain the outperformance of the Equity Income portfolio during the first three months of the year. Admittedly, the period is too brief to place much emphasis upon, but the question has been asked frequently, so we'll offer up a few observations.

From an overarching perspective, value-oriented stocks performed better then growth and momentum stocks during the quarter. This was a reversal of the trend a year earlier and a condition that benefited our style of investing. We also believe dividend stocks entered the year oversold and undervalued, pressured by the prospect of a rising interest rate environment in 2015. Such positioning likely eased during the quarter following the Federal Reserve's more "dovish" commentary regarding the pace and trajectory of future interest rate moves, and allowed dividend-paying stocks to perform better than the overall market.

The best performing sectors in the S&P 500 were telecommunications and utilities. Both sectors saw gains in the mid-teens, which were far in excess of the returns generated by other S&P 500 sectors. The Equity Income portfolio had no exposure to the telecom sector and only an equal weight exposure to the utility sector. As a result, the portfolio's strong gains were not from overexposure to the best performing sectors of the market.

As we've said many times over the years, we work hard to construct this income-generating portfolio with quality companies that would warrant an investment even if they didn't pay a dividend. While there were some underlying trends that helped performance during the period, security selection played the leading role as the portfolio outperformed the S&P 500 in seven of 10 sectors.

The most dramatic sector outperformances during the period came from the industrial, consumer discretionary and energy sectors. Top performing holdings within these sectors included: Mattel, CH Robinson, Fastenal, Graco and Kinder Morgan.

Two S&P 500 sectors were down in the first quarter; financials and health care. The financial companies within the Equity Income portfolio actually appreciated during the period, driven by gains in Iron Mountain, Digital Realty and Progressive. While health care was the worst performing sector within the portfolio and the only sector to show a year-to-date decline, the decline was modest and substantially better than the performance of the broader health care sector as represented by the S&P 500 Index.

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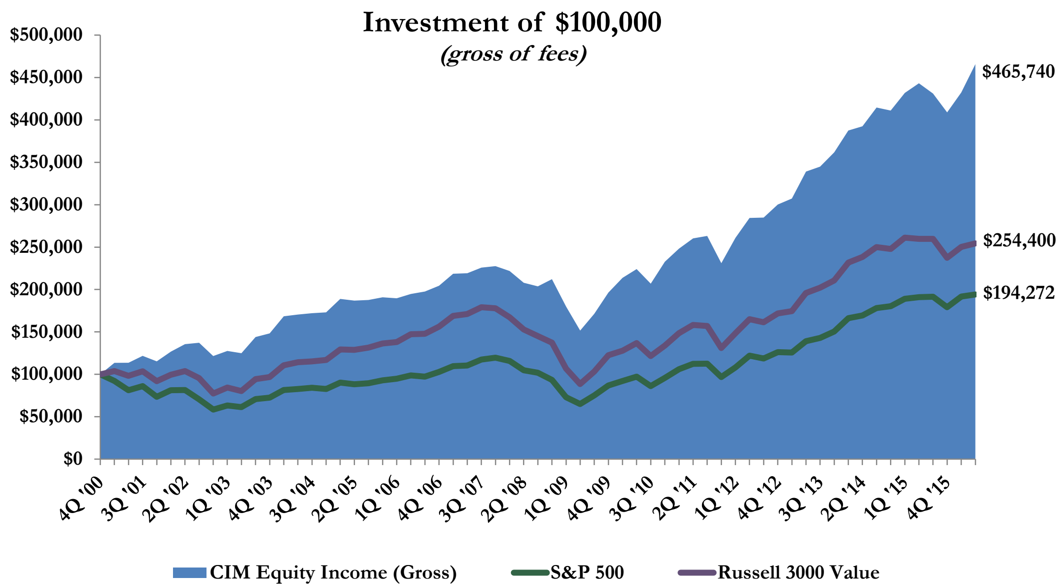
Top 10 Portfolio Holdings (as of 3/31/16)

Company	Market Capitalization	Portfolio Weight
	($ billions)	
Progressive Corp.	20.5	3.4%
Martin Marietta Materials, Inc.	10.3	3.4%
The Kraft Heinz Company	95.5	3.4%
Microsoft Corp.	436.8	3.3%
General Electric Company	295.2	3.3%
3M Company	100.9	3.3%
Fastenal Company	14.1	3.2%
Graco Inc.	4.6	3.2%
Southern Company	47.2	3.2%
Iron Mountain Inc.	7.2	3.1%



Confluence Investment Management LLC

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