Confluence INVESTMENT MANAGEMENT

THIRD QUARTER 2021

International Developed • International Equity Strategies

International Developed invests primarily in large cap, growth-oriented companies in developed markets (excluding U.S.). The strategy's management team employs both top-down and bottom-up fundamental analysis to identify attractive countries and economic sectors as well as high-quality companies worthy of a long-term investment allocation. The portfolio's primary objective is long-term capital appreciation.

Market Commentary

As the season switches to fall, it is easy to become awestruck by the bright red of a burning bush or the burnt orange and vivid yellow of leaves turning on a tree. Sometimes, we become so enamored with a single illustration of natural beauty that we forget to step back and view Mother Nature's entire canvas before us. This analogy can be used to explain the demeanor surrounding international equity markets. Far too often, the total picture can be blurred by a few tantalizing news headlines rather than the complete backdrop. For example, storylines involving international stocks have been dominated by what is happening in China, the energy crisis facing Europe, and changes in leadership within Germany and Japan. One could easily assume that developed market stocks outside the domestic market must be in disarray. However, the opposite is true. On a year-to-date basis, the MSCI EAFE Index through September 30 has recorded a return of +8.3%, well ahead of the average nine-month return this index has posted over the past 10 years (+3.1%). So, despite the many issues surrounding foreign developed markets, performance remains robust.

The relative attractiveness of foreign developed stock markets also continues to improve. The Price/Earnings ratio of the MSCI EAFE Index at the end of the quarter was 18.5, nearly matching its 10-year historical average. This is a dramatic improvement from six months ago when the same measure of P/E was 35% above the historical average. The "E," or earnings component of this ratio, has steadily improved as economies return to normal following pandemic-forced closures. For reference, the P/E ratio of the S&P 500 remains nearly 40% above its 10-year average.

Another tailwind for international developed markets outside of the U.S. comes in the form of rising dividend yields. In March 2020, the MSCI EAFE Index offered investors a yield of 4%. It was nearly halved as a result of suspended dividend payments during the pandemic. However, on July 23, the European Central Bank (ECB) decided not to extend its recommendation that all banks limit dividends beyond September 2021. Since Financials make up a considerable amount of this benchmark (more than 17%), this should help to ensure that yields rise closer to the pre-pandemic level. Currently, the yield on the MSCI EAFE Index stands at 2.5%.

Flows into foreign developed and emerging market equities remained strong during the quarter Should equity investors, as they have recently, turn favor toward more cyclical and value-esque stocks, developed markets outside the U.S. are likely to benefit. The combined allocation of Financials and Industrials is 33% within the benchmark construct, and both of these sectors outperformed during the third quarter. Another critical development is that during the summer months the vaccination rate of the world's developed market population outside the U.S. has risen significantly. We believe that the higher vaccination rates in Europe and Japan will support durable economic recoveries. Capital Economics' latest forecast for 2022 GDP growth remains well above average for the world's advanced economies. Additionally, they forecast equity market returns for Germany, the United Kingdom, and Japan to exceed that of the U.S. next year.

One persistent headwind that has stubbornly remained entrenched is the strength of the U.S. dollar (USD). The Dollar Index strengthened by 1.9% during the past quarter and has now rallied by 4.8% so far in 2021. We continue to believe that the USD will weaken for an extended period of time, although this has admittedly taken longer than we initially expected.

Quarterly Trading Summary

One change was made to the portfolio holdings near the end of the quarter as we decided to exit the position in Melco Resorts & Entertainment (MLCO). Casino, restaurant, and resort operator Melco (bought in March 2019) was certainly not immune to the cessation of leisure travel brought on by the COVID-19 pandemic. Melco took aggressive action to streamline its operations and spending to protect balance sheet integrity with its income flatlining by mandated casino shutdowns. However, during the past 12 months, conditions have slowly, but steadily, improved. As conditions improved, the Macau government announced on September 14 that it planned to increase regulation and oversight on gaming companies. Melco, along with the rest of the gaming stocks in Macau, fell dramatically on this news; MLCO lost 14% on that day. With an ever-uncertain regulatory environment, coupled with rising coronavirus infections, we decided to exit this position.

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Performance Review

International developed market equities began the third quarter by recording positive returns during both July and August. However, global equities sold off during September (the MSCI EAFE Index was -2.9% for the month) as investors showed disquiet over a multitude of headwinds. These included geopolitical tensions, political uncertainty, inflationary pressures, the Delta variant, supply chain disruptions, and regulatory complications, among others. Additionally, the month of September has historically proven to be the worst single month of performance during the calendar year. Against this backdrop, the MSCI EAFE Index posted a return of -0.4%, while the Confluence International Developed strategy recorded a return of -1.0% (gross of fees) during the third quarter. Growth and Value stocks performed largely in line with one another during the past three months as did the constituents of the MSCI EAFE Quality Index.

Year-to-date, the Confluence International Developed strategy recorded a return of +10.0% (gross of fees) versus +8.3% for the MSCI EAFE Index. [*Net-of-fees returns for the same periods were -1.7% QTD and +7.6% YTD. See disclosures on p.4 for fee description; actual investment advisory fees may vary.*]

The two best-performing countries within the portfolio on an absolute basis were Israel (+21.2%) and Denmark (+6.8%), and the worst returns were recorded by Hong Kong (-13.0%) and France (-7.3%). From a sector standpoint, Energy (+10.0%) and Health Care (+3.0%) were the strongest sectors during the quarter, while Communication Services (-16.8%) and Materials (-8.2%) were the weakest.

The top contributors and detractors thus far year-to-date:

Security	Avg Weight (%)	Contribution (%)
Top 5		
DSV Panalpina A/S	4.85	1.73
Icon plc	4.43	1.41
GW Pharmaceuticals plc	0.21	1.29
Novo Nordisk A/S	2.71	0.93
Accenture plc	3.56	0.79
Bottom 5		
Novartis AG	2.08	(0.26)
Melco Resorts & Entertainment Limited	*Sold*	(0.33)
Smith & Nephew plc	1.88	(0.34)
Jazz Pharmaceuticals plc	1.66	(0.35)
Nintendo Company Limited	2.17	(0.64)

(Contribution data shown from a sample account, based on individual stock performance and portfolio weighting)

What We Are Watching

There are many noteworthy topics we are tracking as we enter the final stages of 2021. During the past few months, the Chinese economy has entered an updated model of governance crafted by President Xi Jinping in conjunction with the current membership of the Chinese Communist Party. This has included onerous new regulations placed on many of China's most prolific and powerful companies and implemented under the objective of wealth re-distribution, or "common prosperity." This edict comes at a time when the country is coping with heightened levels of COVID-19 infections and recovery efforts sustained from massive flooding. China is also adding to its internal consternation by taking provocative actions against Taiwan, including invasion of airspace by military aircraft and issuing warnings to Western nations to refrain from interference between the two countries. Relations between the U.S. and China remain intense, although the early October meetings between high-level officials from both sides and the scheduling of a virtual meeting between President Xi and President Biden may signal at least a temporary reprieve in tensions. Chinese authorities are also dealing with the fallout from highly indebted property developer Evergrande as the company's inability to make interest payments has roiled equity markets globally.

Elsewhere, Japanese Prime Minister Yoshihide Suga abruptly resigned in early September over his "poor" handling of Japan's COVID-19 crisis. Fellow Liberal Democratic party member, Fumio Kishida, is now Japan's prime minister. He pledges to implement a COVID stimulus program and bolster Japan's defense forces in order to offset the growing threat from China's regional aggression. Germany's longstanding chancellor, Angela Merkel, finally stepped down after 16 years. Her hand-chosen successor, Armin Laschet, failed to garner enough votes and lost the election to rival party member (Social Democratic Party) Olaf Scholz. While Scholz's party did not win enough seats to form its own government, negotiations are underway with the German Greens party and the Free Democrats. As Scholz attempts to cobble together a government amid the fractured German state, the dearth of experience left behind by Merkel's absence will certainly impact the country.

What We Are Watching continued...

The recovery from the COVID-19 pandemic has created, both in China and Europe, a surge in demand for energy. A lack of coal stockpiles and pressures from a large swath of the investment community to eschew so-called dirty energy (coal, natural gas, oil) in favor of green energy (wind and solar) has created a significant shortfall in the power supply. It has caused a meteoric rise in the price of natural gas within the European continent and the necessity for rolling blackouts in China. It has curtailed production, dented consumer spending, and added to a long list of headwinds facing global supply chains. Confluence Investment Management publishes a *Weekly Energy Report* on Thursdays that provides an in-depth analysis of this phenomenon; the latest report can be found **here**.

While the aforementioned topics have been well documented, Confluence Chief Market Strategist Bill O'Grady and the Confluence macro team also offer insight into areas not in the limelight that will probably shape global equity markets during the months ahead. They address how we are collectively working our way out of a global pandemic, which has created questions regarding which effects are temporary versus permanent. Global supply chains were put almost simultaneously on pause and then largely expected to re-start on cue. This has not happened. Instead, supply chains have been disrupted by sudden demand increases without the supporting supply of labor, transportation, and materials sufficiently available to do so. This has led to inflationary pressures not experienced in recent decades. Globally, investors have become accustomed to annualized inflation varying between 1% and 2%. While some of these pressures are certain to abate during the next several quarters, there remains a possibility that inflation may settle at levels above what most of us have recently experienced.

Second, the macro team points out that the demise of U.S. hegemony is happening rapidly. The result is that corporations will likely have to build redundancy into their supply chains. Globalization promoted setting up shops where output could be generated with the lowest cost and highest productivity. This trend is not likely to continue. Instead, companies will face the decision to re-shore production to protect against foreign intrusion or, at best, regionalize production facilities. Not only would these scenarios create the potential for inefficiency, but they are certain to raise capital expenditures and reduce margins during the build-out phase.

Finally, our research suggests that the single largest risk or opportunity for investors may well be how to position themselves properly, considering the unprecedented amount of liquidity awash globally. While some central banks have begun to reduce stimulus by tapering and/or raising interest rates, the cost of capital remains historically cheap. We continuously discuss these topics in order to make the most informed, long-term investment decisions on behalf of our clients. We welcome questions and conversations on any of these topics.

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(as of 9/30/21)

10 Largest Holdings	Weight
DSV Panalpina A/S	4.4%
Novo Nordisk A/S	4.0%
Diageo plc	3.3%
Icon plc	3.2%
AIA Group Ltd.	3.2%
Shopify Inc.	3.1%
Accenture plc	3.1%
DBS Group Holdings Ltd.	3.1%
Brookfield Asset Management Inc.	3.0%
Willis Towers Watson Public Ltd. Co.	2.9%

Sector Allocation	Weight
Financials	21.5%
Health Care	17.4%
Industrials	16.0%
Information Technology	15.6%
Consumer Staples	8.1%
Consumer Discretionary	7.8%
Materials	6.5%
Energy	2.5%
Communication Services	2.5%
Cash	2.1%

10 Largest Countries	Weight
Canada	15.4%
Switzerland	13.7%
Ireland	13.7%
United Kingdom	11.5%
Japan	8.8%
Denmark	8.4%
France	6.4%
Singapore	5.2%
Germany	5.1%
Sweden	4.4%

The listing of "10 Largest Holdings" is not a complete list of all stocks in the portfolio or which Confluence may be currently recommending. Application of the investment strategy as of a later date will likely result in changes to the listing. Listings of countries and holdings do not represent all of the countries/stocks currently or previously owned in the portfolio or which Confluence may be currently recommending. Sector/country weightings and holdings of individual client portfolios in the program may differ, sometimes significantly, from these listings. Contact Confluence for a complete list of holdings.

All investments carry a certain degree of risk, including possible loss of principal. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager. Equity securities are subject to market risk and may decline in value due to adverse company, industry or general economic conditions.

Performance Composite Returns (For Periods Ending September 30, 2021)

	Pure Gross-of-Fees[1]	Net-of-Fees[2]	MSCI EAFE
Since 10/1/99	5.8%	2.6%	4.5%
20-Year*	7.6%	4.4%	6.6%
15-Year*	5.8%	2.7%	4.1%
10-Year*	9.3%	6.0%	8.1%
5-Year*	11.5%	8.2%	8.8%
3-Year*	11.2%	7.9%	7.6%
1-Year	26.2%	22.4%	25.7%
YTD	10.0%	7.6%	8.3%
QTD	(1.0%)	(1.7%)	(0.4%)

**Average annualized returns*

Calendar Year	Pure Gross-of-Fees[1]	Net-of-Fees[2]	MSCI EAFE	Difference (Gross-MSCI EAFE)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	MSCI EAFE 3yr Std Dev	Composite Dispersion
1999**	26.0%	25.0%	17.0%	9.0%	506	$204,990	-	N/A	N/A	N/A
2000	(12.7%)	(15.3%)	(14.2%)	1.5%	339	$94,891	-	N/A	N/A	3.1%
2001	(20.2%)	(22.5%)	(21.4%)	1.3%	216	$52,064	-	N/A	N/A	2.0%
2002	(20.0%)	(22.4%)	(15.9%)	(4.1%)	181	$39,739	-	16.9%	16.0%	1.1%
2003	37.2%	33.1%	38.6%	(1.4%)	168	$35,515	-	17.9%	17.8%	1.1%
2004	15.9%	12.4%	20.2%	(4.4%)	191	$42,465	-	15.5%	15.4%	0.9%
2005	16.7%	13.2%	13.5%	3.2%	176	$37,524	-	11.4%	11.4%	0.8%
2006	23.9%	20.2%	26.3%	(2.4%)	243	$62,300	-	10.5%	9.3%	0.8%
2007	19.1%	15.6%	11.2%	8.0%	269	$75,983	-	10.5%	9.4%	1.4%
2008	(38.2%)	(40.0%)	(43.4%)	5.2%	256	$43,507	-	18.9%	19.2%	1.2%
2009	22.5%	18.8%	31.8%	(9.3%)	235	$47,380	-	21.7%	23.6%	1.7%
2010	15.3%	11.8%	7.8%	7.5%	206	$47,360	-	23.4%	26.2%	0.8%
2011	(9.7%)	(12.3%)	(12.1%)	2.5%	164	$31,229	-	20.0%	22.4%	0.7%
2012	16.5%	13.0%	17.3%	(0.8%)	154	$34,823	-	17.3%	19.4%	0.6%
2013	20.9%	17.4%	22.8%	(1.8%)	174	$47,418	-	14.5%	16.3%	0.5%
2014	(0.4%)	(3.4%)	(4.9%)	4.5%	116	$34,435	-	11.0%	13.0%	0.7%
2015	(2.3%)	(5.2%)	(0.8%)	(1.5%)	53	$19,412	-	11.3%	12.5%	0.3%
2016	(5.1%)	(8.0%)	1.0%	(6.1%)	30	$7,163	-	11.8%	12.5%	0.4%
2017	23.4%	19.7%	25.0%	(1.7%)	25	$6,957	-	11.0%	11.8%	0.3%
2018	(14.4%)	(17.0%)	(13.8%)	(0.6%)	2	$352	$5,486,737	11.7%	11.2%	0.1%
2019	29.6%	25.7%	22.0%	7.6%	1	$261	$7,044,708	12.4%	10.8%	N/A
2020	15.9%	12.4%	7.8%	8.0%	1	$241	$6,889,798	19.3%	17.9%	N/A

Portfolio Benchmarks

MSCI EAFE (Net) Index – Free float-adjusted market capitalization index designed to measure developed market equity performance, excluding the U.S. and Canada. Performance results presented net of estimated foreign withholding taxes on dividends, interest and capital gains. *(Source: Bloomberg)*

(Prior to March 31, 2020, the S&P/BNY Developed Market ADR Index was shown as a secondary benchmark. This index was removed to simplify the presentation, being less widely recognized and relevant than the primary benchmark. An index is unmanaged and does not incur management fees, transaction costs or other expenses associated with separately managed accounts. It is not possible to invest directly in the index.)

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, 2020. 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 International Developed Strategy was incepted on April 1, 1992, and the current International Developed Composite was created on May 1, 2018. Performance presented prior to May 1, 2018, occurred while the Portfolio Management Team was affiliated with a prior firm and was independently verified for the periods of 10/1/1999 through 12/31/2017. The Portfolio Management Team members were the primary individuals responsible for selecting securities to buy and sell. Composite performance is typically net of foreign withholding taxes on dividends, interest income and capital gains with some exceptions based on custodian treatment. 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 U.S. Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

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

[2] Net-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 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. Prior to year-end 2018, the annual composite dispersion was an asset-weighted standard deviation calculated for 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 International Developed Composite contains fully discretionary International Developed wrap accounts. The International Developed portfolio invests in U.S.-listed shares of large capitalization, non-U.S. companies from developed markets. **Results shown for the year 1999 represent partial period performance from October 1, 1999, through December 31, 1999. 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.

Individual holding performance and contribution methodology as well as a list of every holding's contribution to the strategy can be obtained by contacting Confluence. *Material is published solely for informational purposes and is not an offer to buy or sell or a solicitation of an offer to buy or sell any security or investment product. Top 5 contributors/detractors reflects the strategy's best and worst performers, 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. Sector and country allocations represent a portion currently or previously held in a representative (model) portfolio invested in accordance with the stated investment strategy. Information is presented as supplemental information to the disclosures required by GIPS® standards. Opinions and estimates are as of a certain date and subject to change without notice. Investment or investment services mentioned may not be suitable to an investor and the investor should seek advice from an investment professional, if applicable. Past performance is no guarantee of future results. Investing in securities involves the risk of loss of the amount invested that investors should be prepared to bear. There can be no assurance that any investment objective will be achieved or that any investment will be profitable or avoid incurring losses.* ***Indices:*** *The MSCI EAFE Index is shown as additional information. This index is unmanaged. An investor cannot invest directly in an index. It is shown for illustrative purposes only & does not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.*