Confluence INVESTMENT MANAGEMENT

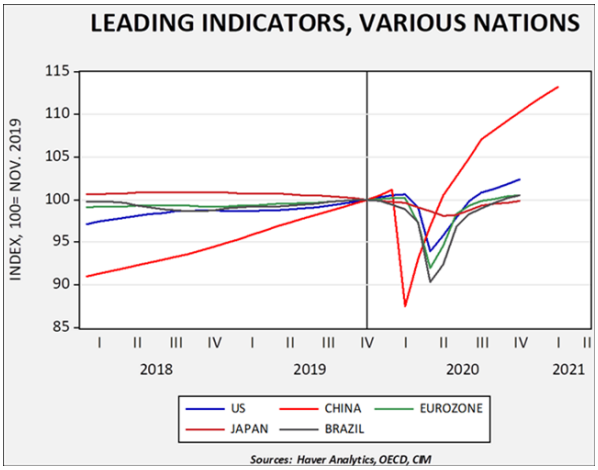
FIRST QUARTER 2021

International Growth • International Equity Strategies

International Growth invests primarily in large cap, growth-oriented companies in both developed and emerging markets. 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. The maximum direct exposure to emerging markets is 25% of the portfolio's total value.

Market Commentary

After more than a year of coronavirus-induced global market disruption and distortions, we are finally beginning to attain a more robust understanding regarding how the post-COVID-19 global macroeconomic recovery will likely take shape. China was the first country to experience the coronavirus pandemic, and it was the first to regain economic momentum. Now, the United States has begun to track a similar path of improvement. What has not yet transpired is a sustained improvement in many of the world's largest economies and geographies, including Japan, much of Europe, Brazil, and most of Latin America, due to continued virus-related shutdowns and scarcity of effective vaccine deployment.



Using Leading Economic Indicator data as compiled by the Organisation for Economic Co-operation and Development (OECD), it is apparent that before the pandemic many of the world's economies were on the path of synchronized economic advancement. It has also become equally clear that the "lockstep" of global recovery is no more. In fact, while conditions are improving both domestically and in China, we expect that the leading indicators for Japan, much of Latin America, and Europe will continue to diverge until the coronavirus pandemic relents in these areas. The recent discovery of adverse side effects from both the AstraZeneca (AZN) and Johnson & Johnson (JNJ) vaccines has confounded efforts to improve conditions in these regions. Capital Economics estimates that suspending the use of these two vaccines will eliminate one-third of the supply available in Europe, further delaying a return to normalcy. As of mid-April, emerging market economies, including Brazil and India, have become the global epicenter(s) of coronavirus outbreaks resulting from inadequate or ineffective vaccine supply and medical health systems stretched beyond capacity. In April, the International Monetary Fund (IMF) updated its World Economic Outlook and provided projections for world output. Unsurprisingly, expectations for both the United States and China were upgraded from October 2020 estimates. The Euro area forecast is now 0.8% lower. Latin America remains projected at 1% above the October estimate, but, in our opinion, there remains a near-term downside risk to this number. While the near-term economic assessment for many of the world's economies remains murky, we expect that rapid and sustained improvement should only be postponed and certainly not canceled. To illustrate this point, Capital Economics has recently updated their 2022 economic forecasts (as of April 9, 2021). The U.S. is expected to expand by 4% next year; however, this is a decline from 6.5% this year. Similarly, China is expected to expand by 3.3% in 2022, but that will be far below the 10% forecast for 2021. Meanwhile, the Eurozone's economic recovery is projected to strengthen in 2022 by 4.5%, an increase from the 3.0% forecast for the balance of this year. Against this projected backdrop, we expect to identify companies in both countries and sectors that will benefit from the multispeed post-pandemic recovery.

Global equities have also begun to experience increased volatility because of inflationary pressure. As of mid-April, crude oil has risen by more than 30%. Commodities, as tracked by the Bloomberg Commodity Index (a basket of commodities including oil, natural gas, hog futures, cotton, coffee, sugar, etc.), are up by 11% since December. The Baltic Dry Index (a measure of the change in costs to ship raw materials) has gained almost 60% in 4.5 months, and 10-year government bonds both domestically and abroad have also risen. The U.S. 10-year Treasury rose from 93 basis points at the end of 2020 to more than 1.6% as of this writing. During the same time frame, the German bond 10-year yield moved from -58 basis points to -31 bps. Globally, the measures of consumer prices and producer prices have also jumped.

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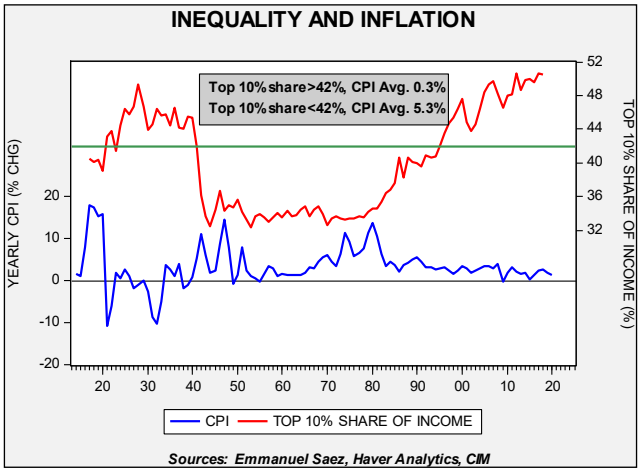
Market Commentary continued...

Further stoking inflationary fears have been the shortage of semiconductors, especially for automakers, and a broader disruption to global supply chains resulting from weather and COVID-19-related shutdowns. While there is ample reason for concern, our base case position is that inflation will remain within asset prices but will not spread to goods. With the populations of most of the world's largest and advanced economies rapidly aging, there is substantial data to support the theory that consumption decreases, in a lasting manner, as consumers age. Additionally, for sustained goods inflation to occur, there must be a change made to address income inequality. The chart below illustrates that when the top 10% earn more than 42% of income, consumer prices average a paltry increase of 0.3%. However, when the top 10% earn less than 42% of total income, the average inflation rate on consumer prices jumps to more than 5%.



So, until the issue of income inequality is substantively addressed, the likelihood of lasting inflation remains low, and the current experience of pricing pressure should subside during the coming months. We'll continue to expand on these and other pertinent investment topics in the coming quarters.

Quarterly Trading Summary

During the quarter , we made one sale and one purchase within the International Growth strategy. In late January, we sold our remaining position of French energy company Total SE and purchased technology company Infosys Limited, headquartered in India. Infosys (INFY) offers technology consulting, outsourcing, and next-generation digital services in verticals that include core banking solutions, artificial intelligence, insurance, automation, and e-commerce. The company began a digital transformation in 2017, and those changes have enabled it to assist its large and diverse customer base (customers located in 46 different countries and include 187 of the Fortune 500 companies) in adapting quickly and efficiently during the coronavirus pandemic. Since 2017, Infosys has increased its return on equity, earnings per share, return on invested capital, and free cash flow, and it trades with more attractive metrics (dividend yield, EV/EBITDA, and P/E) than the average Information Technology company within the index. Additionally, the company has published an ESG Vision for 2030 and became carbon-neutral during the fiscal year 2020. The purchase of Infosys increases the direct emerging market exposure within the portfolio to 16.25%.

The decision to sell Total (TOT), originally purchased in 2018, was predicated on our desire to decrease the Energy sector exposure to an underweight allocation. While energy equities performed strongly during the past three months, we believe that the mid-to-longer-term outlook for oil is challenged, at best. Automakers, particularly in Europe and China, are being pressured to substantially decrease the production and sale of internal combustion engines in favor of fuel cell automobiles that run on electric, not gasoline. As a result, energy companies are now faced with the difficult decision to continue to explore for new oil discoveries to replace reserves or pivot entirely and focus on cleaner energy and/or renewables. Either way, there is a high likelihood that this transition will cause balance sheet harm. Because Total represented less than a half-position within client accounts, and because Royal Dutch Shell has a larger natural gas and renewables business than Total (18% vs. 11%), we decided to maintain Royal Dutch Shell as the only direct Energy sector allocation. Proceeds from the sale of Total went toward the purchase of Infosys.

Performance Review

International equity markets began 2021 on positive footing as the MSCI World ex-U.S. Index posted a return of 4.0% during the first quarter. The "value" component of the MSCI World ex-U.S. Index substantially outperformed the "growth" stocks within the index (+8.5% versus -0.3%). It was the largest quarter of relative outperformance for the MSCI World ex-U.S. Value over Growth since the fourth quarter of 2016. Additionally, the MSCI World ex-U.S. Value has now outperformed MSCI World ex-U.S. Growth by 17.2% during the past six months, the highest level of outperformance for value versus growth dating back to March-September 2009.

The Confluence International Growth strategy was up 2.2% (gross of fees) in the first quarter. The aforementioned divergence between value and growth accounted for the quarterly underperformance of our growth-oriented portfolio compared to the benchmark. On a one-year trailing basis, the Confluence International Growth strategy has recorded a return of 53.5% (gross of fees) versus 45.9% for the MSCI World ex-U.S. Index. [*Net-of-fees returns for the same periods were +1.5% QTD and +49.0% one-year trailing. See disclosures on p.4 for fee description; actual investment advisory fees may vary.*]

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Performance Review continued...

During the quarter, the two best-performing countries within the portfolio on an absolute basis were Singapore (+14.0%) and Mexico (+12.4%), while the worst returns were recorded by Israel (-20.0%) and Brazil (-18.6%). From a sector standpoint, Energy (+10.7%) and Industrials (+7.6%) were the strongest-performing sectors during the quarter, while Materials (-3.1%) and Health Care (-2.8%) were the weakest.

The top contributors and detractors during the quarter:

Security	Avg Weight (%)	Contribution (%)
Top 5		
DSV Panalpina A/S	4.02	0.64
Taiwan Semiconductor Manufacturing	4.59	0.37
DBS Group Holdings Ltd.	2.20	0.31
Tencent Holdings Ltd.	2.83	0.27
LVMH Moët Hennessy Louis Vuitton	3.75	0.25
Bottom 5		
Novartis AG	2.19	(0.17)
PagSeguro Digital Ltd.	1.19	(0.24)
Kirkland Lake Gold Ltd.	1.61	(0.31)
Nintendo Co., Ltd.	2.47	(0.33)
CyberArk Software Ltd.	3.38	(0.72)

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

What We Are Watching

One topic that is certain to garner more international investor attention as we navigate our way toward Sunday, September 26, is the German federal election. Angela Merkel has decided to end her tenure as German chancellor after 16 years in office. Merkel has served as a stabilizing force for the Eurozone throughout her term. Her party, the Christian Democratic Union (CDU), with its conservative alliance partner, the Christian Socialist Union (CSU), held deliberations to identify the candidate to represent them in elections this fall, finally choosing CDU candidate Armin Laschet. Nevertheless, the intense debates about whom to nominate between the CDU and CSU candidates illustrated the division between party members. A CDU member has held the post of German chancellor for 32 of the past 40 years and a total of 52 years since the party was founded in 1945. The CDU Party is center-left, conservative, and pro-Europe. It has been highly influential, especially during Merkel's term, in setting policy within the European Union. According to *Reuters*, the CDU's main rival party, the Greens (known for being center-right and having strong environmental views), has closed the gap in recent polling, with the CDU/CSU in the lead with 25% of the vote versus 23% for the Greens. We will update this narrative as the election draws nearer.

One variable that has a significant influence on the relative performance of both international and domestic stocks is the U.S. dollar (USD). As we have discussed in the past, when the USD is strong, U.S. stocks have tended to outperform, and when the dollar is weak, non-U.S. securities typically outperform. During the first three months of 2021, the USD strengthened by 2.6%, creating a headwind for international equities. However, through mid-April, the U.S. Dollar Index has again returned to a path of weakening by dropping more than 1.6%. From March of last year, the dollar has declined by 7.4%. While we are not forecasting a dramatic slide in the USD, we continue to believe that the dollar has entered an extended period of weakness versus a basket of foreign currencies that, based on history, could last for several years. If this expectation is correct, international equities should perform well relative to domestic stocks.

Not only do we focus on near- and medium-term market-influencing events, but we also take time to consider what could happen to change market dynamics in the long run. Case-in-point, the People's Bank of China has recently begun testing a digital Chinese yuan. In doing so, China has become the first major country to issue state-sponsored digital currency. Chinese President Xi Jinping has publicly stated his desire for China to be at the forefront of the digital currency evolution. According to a *Wall Street Journal* article, "Beijing is positioning the digital yuan for international use and designing it to be untethered to the global financial system, where the U.S. dollar has been king since World War II." The implementation and use of digital currency will also permit the government to immediately and in real-time track who, what, where, and when it is being used. *Bloomberg News* reported that both Federal Reserve Chair Jerome Powell and Treasury Secretary Janet Yellen support the idea of researching the viability of a digital dollar. She stated, "Too many Americans don't have access to easy payment systems and banking accounts, and I think this is something that a digital dollar, a central bank digital currency, could help with." She also believes it could contribute to the goal of "faster, safer, and cheaper payments." However, Powell added, "it's more important for the U.S., as keeper of the world's most popular reserve currency, to be right rather than first on this front." Confluence Chief Market Strategist Bill O'Grady has spent significant time and effort researching and analyzing the potential geopolitical implications of digital currencies issued by the world's central banks, and he has recently completed a four-part series detailing his findings (published March 15 through April 12, 2021). Part I examines what money is, while Part II discusses the current state of money and shows how Central Bank Digital Currencies (CBDC) can act as money in multiple ways. Part III explores the geopolitics surrounding the introduction of digital currencies, and finally Part IV explores the potential market ramifications that CBDCs may create. A link to these ***Weekly Geopolitical Reports***, as well as a multitude of other research and reports, can be found on our **website**.

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(as of 3/31/21)

10 Largest Holdings	Weight
DSV Panalpina A/S	4.4%
Taiwan Semiconductor Manufacturing	4.2%
Sony Corporation	4.0%
Accenture plc	3.7%
Shopify Inc.	3.5%
Icon plc	3.3%
Aptiv PLC	3.2%
Waste Connections, Inc.	3.0%
AIA Group Ltd.	3.0%
CyberArk Software Ltd.	2.9%

Sector Allocation	Weight
Information Technology	22.5%
Industrials	15.6%
Financials	14.2%
Consumer Discretionary	13.1%
Health Care	10.7%
Consumer Staples	9.2%
Materials	7.0%
Communication Services	5.1%
Energy	1.5%
Cash	1.0%

10 Largest Countries	Weight
Canada	15.6%
Ireland	13.8%
Japan	10.5%
Switzerland	7.7%
Denmark	6.7%
United Kingdom	6.7%
China	6.6%
France	5.7%
Singapore	4.3%
Taiwan	4.2%

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 March 31, 2021)

	Pure Gross-of-Fees[1]	Net-of-Fees[2]	MSCI World ex-US
Since 10/1/99	6.8%	3.6%	4.5%
20-Year*	7.7%	4.5%	5.6%
15-Year*	6.7%	3.6%	4.1%
10-Year*	6.6%	3.5%	5.2%
5-Year*	11.8%	8.5%	8.9%
3-Year*	11.2%	7.9%	6.3%
1-Year	53.5%	49.0%	45.9%
YTD	2.2%	1.5%	4.0%
QTD	2.2%	1.5%	4.0%

**Average annualized returns*

Calendar Year	Pure Gross-of-Fees[1]	Net-of-Fees[2]	MSCI World ex-US	Difference (Gross-MSCI World ex-US)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	MSCI World ex-US 3yr Std Dev	Composite Dispersion
1999**	26.6%	25.6%	17.4%	9.2%	131	$48,987	-	N/A	N/A	N/A
2000	(15.0%)	(17.6%)	(13.4%)	(1.7%)	58	$15,193	-	N/A	N/A	3.0%
2001	(18.1%)	(20.5%)	(21.4%)	3.3%	42	$7,128	-	N/A	N/A	1.1%
2002	(17.9%)	(20.4%)	(15.8%)	(2.1%)	32	$4,654	-	17.1%	16.1%	0.7%
2003	40.2%	36.1%	39.4%	0.8%	26	$4,642	-	18.1%	17.7%	0.9%
2004	18.7%	15.2%	20.4%	(1.6%)	25	$5,004	-	15.4%	15.3%	1.1%
2005	18.2%	14.7%	14.5%	3.8%	25	$6,651	-	12.1%	11.3%	0.5%
2006	29.5%	25.6%	25.7%	3.8%	35	$11,866	-	11.6%	9.5%	1.1%
2007	23.4%	19.7%	12.4%	10.9%	49	$16,292	-	12.5%	9.7%	2.9%
2008	(37.8%)	(39.6%)	(43.6%)	5.8%	76	$14,221	-	20.7%	19.5%	1.5%
2009	31.8%	27.9%	33.7%	(1.8%)	114	$28,437	-	23.0%	23.9%	2.1%
2010	13.2%	9.9%	8.9%	4.3%	168	$60,558	-	24.3%	26.3%	1.3%
2011	(11.4%)	(14.1%)	(12.2%)	0.8%	253	$80,988	-	20.1%	22.3%	0.6%
2012	16.1%	12.7%	16.4%	(0.3%)	254	$94,222	-	17.6%	19.0%	0.6%
2013	19.1%	15.6%	21.0%	(1.9%)	291	$113,801	-	14.4%	16.0%	0.6%
2014	(1.7%)	(4.6%)	(4.3%)	2.6%	177	$88,982	-	11.4%	12.7%	0.7%
2015	(2.1%)	(5.0%)	(3.0%)	0.9%	191	$81,898	-	11.5%	12.3%	0.4%
2016	(5.1%)	(7.9%)	2.7%	(7.8%)	113	$39,444	-	12.0%	12.3%	0.7%
2017	25.2%	21.4%	24.2%	1.0%	62	$28,303	-	11.1%	11.7%	0.8%
2018	(13.5%)	(16.1%)	(14.1%)	0.6%	30	$15,707	$5,486,737	11.7%	11.1%	0.2%
2019	30.1%	26.3%	22.5%	7.6%	24	$14,419	$7,044,708	12.5%	10.8%	0.3%
2020	20.6%	17.1%	7.6%	13.1%	25	$15,512	$6,889,798	18.0%	18.1%	0.4%

Portfolio Benchmarks

MSCI World ex-U.S. (Net) Index – Free float-adjusted market capitalization index designed to measure developed market equity performance, excluding the U.S. 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 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, 2019. 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 Growth Strategy was incepted on October 1, 1997, and the current International Growth 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 Growth Composite contains fully discretionary International Growth wrap accounts. The International Growth portfolio invests in U.S.-listed shares of large capitalization, growth-oriented, non-U.S. companies from developed markets with up to 25% from emerging 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 World ex-U.S. 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.*