First Quarter

2024

Large Cap Value • Value Equity Strategies

Large Cap Value is focused on seasoned companies that generally have capitalizations above $10 billion. Companies are selected using a bottom-up, fundamental research process that seeks to identify individual businesses that possess substantial competitive advantages and that are trading at discounts to our estimate of intrinsic value. The portfolio typically comprises 23-25 holdings and is expected to result in low to moderate turnover. The strategy is appropriate for clients whose primary objective is capital appreciation and whose secondary objective is dividend income.

Market Commentary

In the first quarter of 2024, the equity markets saw a continuation of the Santa Claus rally that ended 2023, with the S&P 500 Index posting a rare back-to-back quarterly gain in the double-digits. The rally was sparked in late October 2023 when the Federal Reserve signaled the end of policy tightening as the downward trend in inflation (aka disinflation) was expected to continue toward the Fed's target of 2.0%. In short order, market participants were pricing in six interest rate cuts for 2024 (see *Figure 1*), which increased the probability of a soft landing. And although recent datapoints indicate that elevated levels of inflation may be sticky (see *Figure 2*), hence the reduction during the quarter in the number of expected rate cuts to three, the equity markets continued to rally.

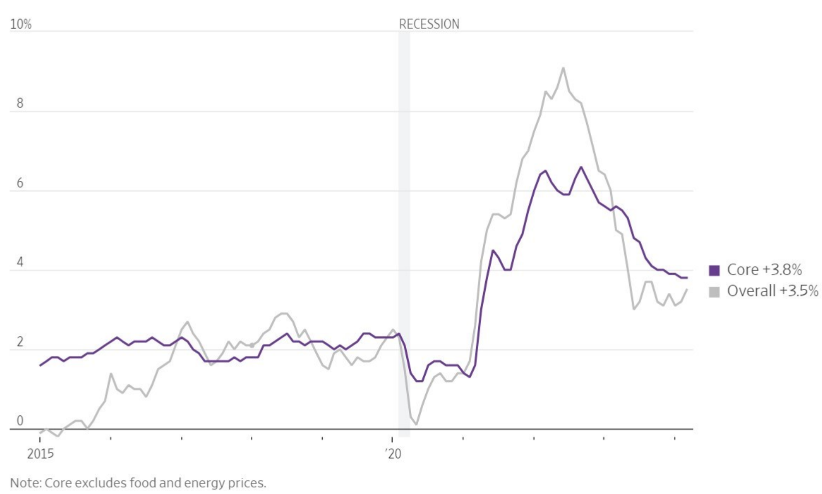
Why would stocks remain strong when elevated inflation data is pointing to the possibility that the Fed will keep rates higher for a longer period? There are a handful of possible reasons, but we suspect it is the belief that the Fed is bluffing on its inflation target. More specifically, investors doubt the validity of the Fed maintaining its stated 2.0% inflation target, believing the Fed will instead settle for a higher inflation target and move forward with rate cuts despite inflation stalling at levels well above 2.0%. This would clearly benefit the economy near-term and support revenue and earnings growth. As a result, we are seeing a continued tailwind for stocks, with the S&P 500 up 10.6% in the first quarter and 28% from the low in late October 2023.

Figure 1 **U.S. Interest Rate (%)**

(Source: Financial Times, 3/19/2024)

Unlike much of the past several years, recent returns have been broader-based. Both large caps and small caps, as measured by the Russell 1000 and 2000 indexes, respectively, are up approximately 30% off the October low. Although growth has outperformed value, the gap was much narrower than the recent past as Apple (AAPL) was up only 2% and Tesla (TSLA) posted a loss of 15.2%, which helped narrow the gap to "only" 5.3%, with the Russell 1000 Growth up 31.4% versus the Russell 1000 Value up 26.1%.

Figure 2 **Consumer Price Index, Change From a Year Earlier**



(Source: Wall Street Journal, 4/10/2024)

See GIPS Report on pages 5-6.

Market Commentary continued...

There are still pockets of excess speculation specifically around artificial intelligence (AI) and cryptocurrency, perhaps best evidenced by two "small cap" names, Super Micro Computer (SMCI) and MicroStrategy (MSTR), which are up +320% from the October low and now sport market capitalizations of $60 billion and $30 billion, respectively. And yet these two companies are still included in the Russell 2000 Index, a small cap index with a median market cap of approximately $956 million, and are impacting the index's returns. Both companies also have checkered histories as SMCI was delisted from the NASDAQ in 2019 for accounting irregularities, while MSTR leader Michael Saylor has used the company's balance sheet to acquire bitcoin (and, more recently, issued stock and convertible bonds to acquire even more bitcoin), all while actively selling his own shares. This revival of bitcoin and the recent Reddit IPO lends further credence to the sense that speculation still abounds.

On the other hand, fixed income markets were more sanguine in light of the recent inflation datapoints, giving back some of their recent gains. Recall that the 10-year Treasury yield fell from 4.98% in late October 2023 to 3.88% by year-end, providing a boost to financial assets and the Santa Claus rally. However, during the first quarter of 2024, the 10-year Treasury yield rose to 4.20% (see *Figure 3*). With inflation remaining at elevated levels, the backup in yields was rather muted and has some pundits pointing to the limited supply of longer-term notes as the Treasury Department shifted refunding to favor short-term bills. This shift helped suppress long-term yields which aided longer-duration bonds as well as stocks. At current levels, the 10-year Treasury is trading more in line with levels preceding the Great Financial Crisis in 2008-09 and provides a real rate of return that has been absent for much of the past 15 years and has benefited financial engineering over operating acumen.

Figure 3 **Market Yield on U.S. Treasury Securities at 10-Year Constant Maturity**

(Source: Federal Reserve Economic Data, 3/31/2024)

Outlook

Thus far, the economy has avoided a recession in the face of a sharp rise in interest rates, while employment has remained strong and inflation levels have been trending downward. This environment has benefited the equity markets; however, the disinflation of the past year and a half appears to be stalling. Thus, the primary focus remains on inflation and how future datapoints will impact the timing and magnitude of Fed actions. While the broadening of the equity markets over the past few months is a positive sign, the strength has outpaced earnings growth which has pushed up valuations and leaves equities susceptible to a pullback. Given the spotlight on inflation, the geopolitical backdrop, with conflicts in Russia/Ukraine, the Middle East, and China/Taiwan, and elections occurring in 2024 for half of the world's population, we anticipate some added volatility which also means opportunities for long-term investors. Of course, we will continue to stay focused on our investment philosophy which has always been centered on business and valuation analysis.

Strategy Commentary

Equity markets continued their climb in the first quarter of 2024, extending a rally that began in late October which was initially sparked by expectations of declining interest rates and inflation. Coming into the year, the consensus forecast implied that the Fed would cut interest rates many times. However, with inflation remaining elevated, those expectations have shifted. The prevailing belief is that the Fed will keep rates higher for longer. Despite this, equities continued to surge in the first quarter.

The market's ascent has continued for five months and is now up 28% from the late October lows. For only the ninth time since 1940, the S&P 500 advanced double-digits in consecutive quarters. On the heels of the fourth quarter's 11.7% increase, the S&P 500 returned 10.6% in the first quarter. The Russell 1000 Value grew 9.0% during the first quarter and the Confluence Large Cap Value strategy was up 8.0% over the same period (gross of fees). [*The strategy's net-of-fees return for the same period was 7.2% QTD. See disclosures on last page for fee description; actual investment advisory fees may vary.*]

We have discussed the outsized impact of the "Magnificent Seven" mega-cap stocks in past commentaries. In Q1, two of these high-flyers struggled to keep pace, with Apple (AAPL) and Tesla (TSLA) down 8% and 30%, respectively. As noted in our Q4 2023 commentary, we may be seeing a broadening of market performance that isn't as highly concentrated in just a few large companies. Except for Real Estate, which is highly sensitive to interest rates, every industry sector saw positive returns in the first quarter. Further, there was not a single sector that dramatically outperformed the rest.

The performance of the Confluence Large Cap Value strategy was broadly in line with the benchmarks. On the heels of outperformance versus the Russell 1000 in the fourth quarter, the strategy slightly trailed during the first quarter of 2024. While we pay attention to quarterly performance, it is not something that consumes much of our thought. We are far more focused on whether our companies are widening their competitive moats and executing on the fundamentals that will build long-term value. We find that quarter-to-quarter fluctuations often contain more noise than signal.

We seek companies with attributes that will allow them to compound value over a time horizon measured in years. These qualities include durable competitive advantages that confer pricing power and the ability to deploy capital at high returns. Further, we look for businesses that are not overburdened by debt and are led by experienced managers. We believe these traits are necessary ingredients for good long-term performance. In addition to scouring the market in search of such businesses, we remain steadfast followers of our existing holdings and monitor them closely to ensure they continue to meet our criteria.

The primary contributors to performance in the first quarter included plumbing and paint manufacturer, Masco Corp. (MAS), and property and casualty insurer, W. R. Berkley Corp. (WRB). The market was encouraged by Masco's recent earnings report, which showed signs that its end-markets are stabilizing. Further, management expressed confidence in better-than-expected profitability targets. W. R. Berkley's stock performed well in the first quarter, with healthy growth in written premiums, prudent underwriting, and sizeable capital return to shareholders in the form of share repurchases and a special dividend.

There were two primary detractors from first quarter performance. The first was Clarivate (CLVT), a subscription-based provider of data and analytics that organizes information related to patents, trademarks, academic studies, and scientific research. We were drawn to this asset at the beginning of 2022 due to its high-margin, recurring revenue characteristics. Although the business suffered from underinvestment during prior ownership, we believed the new leadership team had solid experience leading similar data businesses and a good track record of unlocking shareholder value. Unfortunately, acquisitions made by management have produced inconsistent results and strained the balance sheet. With anemic growth already a frustration, the company recently made a downward revision to its growth goals. This is yet another disappointment and, despite some of its attractive traits, Clarivate may represent a value trap.

The second detractor was Dun & Bradstreet Holdings (DNB), a data aggregation business that serves as a central repository for current and accurate information about companies. Businesses register with Dun & Bradstreet, through the corporate equivalent of a social security number, and readily supply the company with accurate information. This data is used to monitor creditworthiness and financial relationships, allowing companies to extend or receive credit. Operating a trusted network that confers a host of benefits to its constituents is a valuable long-term competitive advantage. Like Clarivate, Dun & Bradstreet had endured mismanagement and a lack of investment. Correcting these issues has suppressed near-term profitability and cash flow, which has negatively impacted the stock's performance. However, these necessary restructuring efforts appear to be bearing fruit, evidenced by expanding multi-year contracts, high retention rates, and revenue growth. Unfortunately, we were likely too early to this investment, but we believe that greater value will be recognized as the company continues to make progress on its transformation. [*See contribution table on page 5.*]

Strategy Commentary continued...

A new addition to the portfolio is Constellation Brands (STZ), a leading producer and importer of some of America's best-selling and fastest growing alcoholic beverage brands. In the US, the company enjoys a near-monopoly position on imported Mexican beer, having acquired the exclusive rights to the Modelo, Corona, and Pacifico brands. A fact that may come as a surprise is that Modelo is now the #1 selling beer brand in the US. Constellation has benefited from population and income growth in its core Hispanic demographic as well as premiumization in the beer category, which have led to industry-leading sales growth, margins, and cash generation. Importantly, we believe the company has undergone a dramatic improvement in senior management and corporate governance that has not been fully appreciated by the market. With continued rationalization of its wine and spirits portfolio to focus on premium, higher-margin offerings, and a renewed focus on the return of capital to shareholders, we believe Constellation Brands is poised to build long-term value.

No holdings were sold from the portfolio during the first quarter. We continue to build another new position, which we look forward to discussing in a future commentary once complete.

Outlook

As always, there is no shortage of events to prognosticate about. What will happen with interest rates, the economy, elections, and geopolitics? Will the market be driven by a handful of enormous companies, or will performance become more broad-based? We are humble students of history and current events; however, we believe the highest return on our efforts is time spent studying businesses and searching for those with attributes that enable multi-year compounding. This is especially important in a more normalized era of positive real interest rates. We are steadfast in our philosophy that owning competitively advantaged businesses, ones that are run by experienced managers and trading at attractive valuations, is a wise long-term orientation.

Contribution[1]

(YTD as of 3/31/2024)

The top contributors and detractors for the portfolio in 2024 are shown in this table:

Security	Avg Weight (%)	Contribution (%)
Top 5		
Masco Corp.	5.70	0.99
W. R. Berkley Corp.	4.25	0.98
Fastenal Co.	4.48	0.84
Oracle Corp.	4.30	0.81
Stryker Corp.	4.21	0.78
Bottom 5		
Keysight Technologies Inc.	4.11	(0.09)
S&P Global Inc.	4.08	(0.13)
Starbucks Corp.	4.09	(0.19)
Dun & Bradstreet Holdings Inc.	1.76	(0.27)
Clarivate plc	1.94	(0.61)

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

Performance Composite Returns[2] (For Periods Ending March 31, 2024)

	Since Inception**	25-Year*	20-Year*	15-Year*	10-Year*	5-Year*	3-Year*	1-Year	YTD	QTD
Large Cap Value *Pure Gross-of-Fees*[3]	11.3%	9.2%	10.3%	14.8%	10.6%	12.3%	8.7%	19.6%	8.0%	8.0%
Max Net-of-Fees[4]	8.2%	6.1%	7.1%	11.4%	7.4%	9.0%	5.4%	16.1%	7.2%	7.2%
S&P 500	10.7%	7.8%	10.1%	15.6%	12.9%	15.0%	11.5%	29.9%	10.6%	10.6%
Russell 1000 Value	9.8%	7.4%	8.3%	13.1%	9.0%	10.3%	8.1%	20.2%	9.0%	9.0%

Calendar Year	Pure Gross-of-Fees[3]	Max Net-of-Fees[4]	S&P 500	R1000 Value	Difference (Gross-S&P500)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	S&P 500 3yr Std Dev	R1000V 3yr Std Dev	Composite Dispersion
1994**	3.4%	2.6%	(0.0%)	(1.6%)	3.4%	122	$10,206		N/A	N/A	N/A	N/A
1995	32.7%	29.1%	37.6%	38.3%	(4.9%)	178	$24,073		N/A	N/A	N/A	1.1%
1996	29.9%	26.4%	23.0%	21.6%	6.9%	417	$63,132		N/A	N/A	N/A	1.7%
1997	31.9%	28.3%	33.4%	35.2%	(1.5%)	973	$151,053		N/A	N/A	N/A	2.1%
1998	9.0%	6.0%	28.6%	15.6%	(19.6%)	2,360	$297,953		N/A	N/A	N/A	1.8%
1999	2.9%	0.1%	21.0%	7.3%	(18.1%)	2,138	$260,171		N/A	N/A	N/A	1.7%
2000	11.5%	8.4%	(9.1%)	7.0%	20.6%	1,104	$159,096		N/A	N/A	N/A	2.3%
2001	(2.5%)	(5.1%)	(11.9%)	(5.6%)	9.4%	1,065	$145,683		N/A	N/A	N/A	1.1%
2002	(12.2%)	(14.6%)	(22.1%)	(15.5%)	9.9%	1,027	$125,161		N/A	N/A	N/A	0.6%
2003	30.9%	27.3%	28.7%	30.0%	2.2%	1,010	$163,840		15.8%	18.1%	16.0%	1.0%
2004	15.7%	12.6%	10.9%	16.5%	4.8%	1,052	$197,447		13.7%	14.9%	14.8%	1.0%
2005	(1.6%)	(4.3%)	4.9%	7.1%	(6.5%)	1,064	$188,332		8.7%	9.0%	9.5%	0.6%
2006	17.8%	14.5%	15.8%	22.2%	2.0%	957	$198,952		5.8%	6.8%	6.7%	0.6%
2007	5.9%	3.0%	5.5%	(0.2%)	0.4%	834	$174,711		6.7%	7.7%	8.1%	0.6%
2008	(27.0%)	(29.1%)	(37.0%)	(36.8%)	9.9%	119	$25,562	$291,644	13.2%	15.1%	15.4%	N/A
2009	28.6%	24.8%	26.5%	19.7%	2.2%	149	$53,387	$533,832	17.7%	19.6%	21.1%	1.4%
2010	12.1%	8.8%	15.1%	15.5%	(3.0%)	192	$76,040	$751,909	19.7%	21.9%	23.2%	0.4%
2011	6.4%	3.2%	2.1%	0.4%	4.3%	228	$89,145	$937,487	17.1%	18.7%	20.7%	0.3%
2012	19.0%	15.4%	16.0%	17.5%	3.0%	249	$143,568	$1,272,265	13.5%	15.1%	15.5%	0.4%
2013	37.6%	33.6%	32.4%	32.6%	5.2%	373	$208,844	$1,955,915	10.6%	11.9%	12.7%	0.9%
2014	10.7%	7.5%	13.7%	13.4%	(2.9%)	618	$278,339	$2,589,024	8.6%	9.0%	9.2%	0.5%
2015	1.6%	(1.4%)	1.4%	(3.8%)	0.2%	858	$352,556	$3,175,419	10.1%	10.5%	10.7%	0.5%
2016	8.6%	5.4%	12.0%	17.3%	(3.4%)	1,003	$396,038	$4,413,659	10.0%	10.6%	10.8%	0.4%
2017	16.1%	12.6%	21.8%	13.6%	(5.7%)	1,049	$380,737	$5,944,479	9.0%	9.9%	10.2%	0.6%
2018	(4.6%)	(7.4%)	(4.4%)	(8.3%)	(0.2%)	1,029	$364,805	$5,486,737	10.4%	10.8%	10.8%	0.6%
2019	34.5%	30.5%	31.5%	26.5%	3.0%	1,118	$525,944	$7,044,708	11.8%	11.9%	11.8%	0.6%
2020	13.0%	9.7%	18.4%	2.8%	(5.4%)	1,229	$647,076	$6,889,798	18.8%	18.5%	19.6%	0.9%
2021	26.8%	23.0%	28.7%	25.1%	(1.9%)	1,251	$738,402	$7,761,687	18.2%	17.2%	19.1%	0.6%
2022	(15.5%)	(18.0%)	(18.1%)	(7.6%)	2.7%	1,274	$609,865	$6,931,635	21.0%	20.9%	21.3%	0.6%
2023	16.9%	13.4%	26.3%	11.4%	(9.4%)	1,281	$611,018	$7,200,019	17.8%	17.3%	16.5%	0.7%

**Average annualized returns* ***Inception is 10/1/1994* *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 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. *(Source: Bloomberg)*

Confluence Value Equities Investment Committee

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Disclosures

Market & Strategy Commentary—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. Opinions and estimates are as of a certain date and subject to change without notice. Past performance is no guarantee of future results.

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Indexes: The S&P 500 and Russell 1000 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.

[1] **Contribution—**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.

[2] **Performance 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, 2022. 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 Large Cap Value Strategy was incepted on October 1, 1994, and the current Large Cap Value Composite was created on August 1, 2008. Performance presented prior to August 1, 2008, occurred while the Portfolio Management Team was affiliated with a prior firm and the Portfolio Management Team members were the primary individuals responsible for selecting the securities to buy and sell. 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.

[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: 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. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Large Cap Value Composite contains fully discretionary Large Cap Value wrap accounts. Large Cap Value is a value-based, bottom-up portfolio that utilizes stocks with market capitalizations typically exceeding $10 billion.

**Results shown for the year 1994 represent partial period performance from October 1, 1994, through December 31, 1994. 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 and/or performance was calculated quarterly prior to January 2001.

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