

Equity Strategies • Small Cap Value

Small Cap Value is focused on companies that generally have capitalizations below \$2 billion. These companies are selected using a bottom-up, fundamental research process that seeks to identify individual businesses that possess competitive advantages and that are trading at substantial discounts to our estimates of intrinsic value. The portfolio typically comprises 30-35 holdings and is expected to result in low to moderate turnover. The strategy is suitable for clients whose primary objective is capital appreciation.

Strategy Commentary

Small capitalization stocks ended the year on a strong note as the Russell 2000 and Russell 2000 Value posted fourth quarter returns of 9.9% and 8.5%, respectively. This capped off a good year for small cap stocks as the Russell 2000 and Russell 2000 Value were up 25.5% and 22.4%, respectively, in 2019. The Small Cap Value strategy also generated solid returns for the quarter, up 8.1%, and ended the year up 27.0% (both gross of fees). *(The strategy was up 7.3% QTD and 23.2% YTD (net of fees). Net of fees calculated using the highest applicable annual bundled fee of 3.00%. See performance disclosures on p.2 for fee description; actual investment advisory fees may vary.)*

The year started with heightened apprehension as investors feared the Federal Reserve would continue its monetary tightening with additional rate increases throughout 2019. At the start of the year market participants were anticipating three additional rate increases which investors feared would cause a recession. FOMC actions and forecasts had elevated investor concerns in the later part of 2018 which resulted in a sharp selloff in the fourth quarter and pushed calendar-year returns into negative territory for 2018, despite strong earnings growth that year. Quite the opposite occurred in 2019 as earnings will likely show a decline in the low single-digits, yet equity returns were extremely strong. The primary culprit was the Fed signaling in early January that patience on tightening was required. This proved to be a prudent course as economic growth remained sluggish amid the trade tariffs and ultimately resulted in the Fed easing, not tightening, monetary policy on three occasions by reducing the fed funds rate. The Fed’s statement in January and its actions throughout the year, including providing liquidity for the repo market, reduced the probability of a recession and boosted investor sentiment.

Small cap returns in 2019 were relatively broad-based, with only the Energy sector posting negative returns; however, the dispersion was quite large. Small Cap Value also saw wide dispersion as businesses were either handsomely rewarded for positive developments or punished for lackluster results. Four

companies in the portfolio announced acquisitions in 2019 (Luxoft, Cambrex, Monotype Imaging and Innophos), with all but Innophos closing during the calendar year.

During the fourth quarter we added James River Group (insurance), while the remaining shares of Potbelly and Raven Industries were sold. The Monotype Imaging and Cambrex acquisitions were completed during the quarter which provided cash to be redeployed.

The top-performing and worst-performing positions during the quarter were as follows:

Security	Avg Weight	Contribution
Top 5		
Cannae Holdings, Inc.	5.23	1.62
i3 Verticals, Inc.	3.20	1.14
Allied Motion Technologies Inc.	3.28	1.07
RE/MAX Holdings, Inc.	3.25	0.62
Kadant Inc.	2.88	0.55
Bottom 5		
RBC Bearings Incorporated	3.33	(0.16)
Gladstone Commercial Corporation	3.37	(0.20)
Avanos Medical, Inc.	2.69	(0.22)
Movado Group, Inc.	2.35	(0.30)
MTS Systems Corporation	2.70	(0.32)

(Contribution data shown from a sample account)

Going forward, the economy continues to advance, albeit at a slower pace than 2018, as the tailwind of fiscal and monetary policies outweigh current trade tensions. We expect modest economic expansion leading to reasonable earnings growth and for inflation and inflation expectations to remain benign, which supports current valuations. While the probability of a recession has increased over the past few months, we don’t foresee one occurring in 2020. As always, we remain focused on company-specific fundamentals and valuations and believe the current market will provide us with opportunities to buy quality companies at reasonable prices.

ABOUT CONFLUENCE INVESTMENT MANAGEMENT LLC

Confluence Investment Management is an independent Registered Investment Advisor located in St. Louis, Missouri, that provides professional portfolio management and advisory services to institutional and individual clients. Confluence’s investment philosophy is based upon independent, fundamental research that integrates evaluation of market cycles, macroeconomics and geopolitical analysis with the firm’s value-driven, company-specific approach. The portfolio management philosophy begins by assessing risk and follows through by positioning clients to achieve their income and growth objectives.

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10 Largest Holdings (as of 12/31/19)

Company	Market Capitalization (\$ billions)	Portfolio Weight
Cannac Holdings, Inc.	2.94	5.3%
Frontdoor, Inc.	4.01	4.3%
Morningstar, Inc.	6.48	3.9%
i3 Verticals, Inc.	0.77	3.7%
Allied Motion Technologies Inc.	0.47	3.6%
SJW Group	2.02	3.6%
RE/MAX Holdings, Inc.	0.69	3.6%
Northwest Natural Holding Co.	2.24	3.4%
Thermon Group Holdings, Inc.	0.88	3.4%
John Bean Technologies Corp.	3.57	3.2%

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. Sector 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 12/31/19

	Pure Gross-of-Fees ¹	Net-of-Fees ²	R2000	R2000 Value	Calendar Year	Pure Gross-of-Fees ¹	Net-of-Fees ²	R2000	R2000 Value	Difference (Gross-R2000)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	R2000 3yr Std Dev	R2000V 3yr Std Dev	Composite Dispersion
Since Inception**	12.2%	9.0%	9.2%	9.9%	1994**	(3.3%)	(3.9%)	(1.9%)	(3.0%)	(1.4%)	389	\$41,690		N/A	N/A	N/A	N/A
					1995	24.2%	20.8%	28.4%	25.8%	(4.3%)	267	\$34,667		N/A	N/A	N/A	0.8%
25-Year*	12.5%	9.3%	9.3%	10.1%	1996	20.7%	17.4%	16.5%	21.4%	4.2%	249	\$39,188		N/A	N/A	N/A	1.0%
20-Year*	12.0%	8.8%	7.6%	9.4%	1997	46.5%	42.5%	22.4%	31.8%	24.1%	353	\$63,832		N/A	N/A	N/A	1.1%
15-Year*	10.3%	7.0%	7.9%	6.9%	1998	(4.2%)	(6.8%)	(2.5%)	(6.5%)	(1.6%)	1,080	\$111,513		N/A	N/A	N/A	1.7%
10-Year*	12.9%	9.5%	11.8%	10.6%	1999	(7.1%)	(9.6%)	21.3%	(1.5%)	(28.4%)	745	\$69,869		N/A	N/A	N/A	1.2%
5-Year*	11.0%	7.7%	8.2%	7.0%	2000	34.4%	30.7%	(3.0%)	22.8%	37.4%	374	\$47,699		N/A	N/A	N/A	1.7%
3-Year*	11.5%	8.2%	8.6%	4.8%	2001	12.6%	9.6%	2.5%	14.0%	10.1%	395	\$56,254		N/A	N/A	N/A	0.7%
1-Year	27.0%	23.2%	25.5%	22.4%	2002	(11.4%)	(13.8%)	(20.5%)	(11.4%)	9.1%	434	\$48,944		N/A	N/A	N/A	0.7%
YTD	27.0%	23.2%	25.5%	22.4%	2003	36.2%	32.5%	47.3%	46.0%	(11.1%)	464	\$71,199		15.4%	21.6%	18.4%	0.9%
QTD	8.1%	7.3%	9.9%	8.5%	2004	23.2%	19.9%	18.3%	22.2%	4.9%	572	\$101,835		12.7%	19.0%	17.5%	1.4%
					2005	8.2%	5.3%	4.6%	4.7%	3.6%	722	\$111,469		9.0%	15.1%	14.1%	1.6%
					2006	19.1%	15.9%	18.4%	23.5%	0.8%	694	\$117,282		7.1%	13.8%	12.3%	1.1%
					2007	(1.7%)	(4.4%)	(1.6%)	(9.8%)	(0.1%)	543	\$84,018		7.5%	13.2%	12.6%	1.1%
					2008	(21.8%)	(24.0%)	(33.8%)	(28.9%)	12.0%	61	\$8,568	\$291,644	14.0%	19.8%	19.1%	N/A
					2009	29.6%	25.8%	27.2%	20.6%	2.4%	54	\$9,823	\$533,832	20.9%	24.8%	25.6%	2.3%
					2010	24.6%	20.9%	26.9%	24.5%	(2.3%)	83	\$19,208	\$751,909	23.3%	27.7%	28.4%	1.5%
					2011	(0.9%)	(3.8%)	(4.2%)	(5.5%)	3.3%	85	\$18,032	\$937,487	21.8%	25.0%	26.0%	1.2%
					2012	16.0%	12.6%	16.3%	18.1%	(0.4%)	105	\$26,346	\$1,272,265	15.6%	20.2%	19.9%	0.3%
					2013	27.4%	23.6%	38.8%	34.5%	(11.5%)	113	\$31,217	\$1,955,915	12.2%	16.4%	15.8%	0.5%
					2014	9.3%	6.1%	4.9%	4.2%	4.4%	140	\$34,077	\$2,589,024	8.6%	13.1%	12.8%	0.6%
					2015	(1.7%)	(4.7%)	(4.4%)	(7.5%)	2.7%	158	\$34,928	\$3,175,419	10.3%	14.0%	13.5%	0.4%
					2016	23.7%	20.0%	21.3%	31.7%	2.4%	198	\$56,608	\$4,413,659	11.6%	15.8%	15.5%	1.2%
					2017	19.5%	16.0%	14.6%	7.8%	4.9%	354	\$103,862	\$5,944,479	10.8%	13.9%	14.0%	0.9%
					2018	(8.6%)	(11.3%)	(11.0%)	(12.9%)	2.5%	400	\$88,885	\$5,486,737	13.1%	15.8%	15.8%	0.8%
					2019	27.0%	23.2%	25.5%	22.4%	1.5%	449	\$124,071	\$7,044,708	14.5%	15.7%	15.7%	0.8%

*Average annualized returns

**Inception is 10/1/1994

Portfolio Benchmarks

Russell 2000® Index – A capitalization-weighted index measuring performance of approximately 2,000 companies in the Russell 3000® Index.

Russell 2000® Value Index – A capitalization-weighted index designed to measure performance of those Russell 2000® Index companies with lower price-to-book ratios and lower forecasted growth values.

(Source: Bloomberg)

Confluence claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Confluence has been independently verified for the periods of 8/1/2008 through 12/31/2018. A copy of the verification report is available upon request. Verification assesses whether: 1. the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis, and 2. the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation. The Small Cap Value Strategy was inceptioned on October 1, 1994 and the current Small 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.

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 (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. Additional information regarding policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. The annual composite dispersion is an equal-weighted standard deviation calculated for accounts in the composite for the entire year. The Small Cap Value Composite contains fully discretionary Small Cap Value wrap accounts. Small Cap Value is a value-based, bottom-up portfolio that utilizes stocks with a market capitalization typically less than \$2 billion. *Smaller capitalization companies, due to their size, are generally more vulnerable to adverse general market or economic developments than larger, more established companies.* **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 Jan 2001.

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. Holdings identified do not represent all of the securities purchased, sold or recommended. 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 Russell 2000 and Russell 2000 Value Indexes are shown as additional information. These indices 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.