

## Mid Cap Core Portfolio

### First Quarter 2017



### Portfolio Review

The Mid Cap Core portfolio outperformed the Russell Midcap Index during the first quarter. The outperformance was primarily driven by positive stock selection in the materials and producer durables sectors. Negative stock selection in the consumer discretionary and financial services sectors detracted from performance.

Positions that contributed most positively to performance during the quarter were Skyworks Solutions and Globus Medical. Skyworks Solutions saw improved momentum in its business, with a recovery from its Apple inventory oversupply missteps. The company strengthened its relationships with customers outside of Apple, most notably in China. While customer concentration is a persistent concern, the company's technology appears to be helping it to drive content gains in new generations of devices. Globus Medical focuses on the design and development of musculoskeletal implants for patients with spinal disorders. After Globus Medical saw its revenues disappoint the past three quarters due to sales force issues, revenues improved in the fourth quarter of 2016 with these headwinds abating. The company continues to develop its robotic and trauma products, which we believe offers longer-term revenue drivers.

Positions that contributed most negatively to performance during the quarter were Sally Beauty Holdings and First Financial Bankshares. Sally Beauty continues to struggle through its retail turnaround, which to date has been more disruptive than helpful to driving sales. The company has maintained its core loyal shoppers, but is struggling to drive new traffic to the stores. The new management team continues to implement new initiatives, such as a new loyalty program, social media marketing and product brands launches. Eventually, we believe this will gain traction and support more sustainable results. The stock has also been pressured by fears that the core professional business could weaken. Management is working to ensure there is enough newness and core product to sustain its strong professional business. First Financial Bankshares increased meaningfully at the end of last year, as higher oil prices improved the prospect for some of its customers, in addition to the expectation for less regulation and higher interest rates under the Trump administration. From a fundamental perspective, the most recent quarter's results were typical for First Financial with modest loan and earnings growth. However, the share price still declined throughout the quarter, as positive investor sentiment for banks under the new Trump Administration has waned.

### Purchases and Sales

During the quarter, we purchased Lennox International and sold our position in Edwards Lifesciences.

Lennox manufactures a wide variety of heating, ventilation, air conditioning (HVAC) and refrigeration products. The company consists of three segments: Residential, Commercial and Refrigeration. Lennox has an established brand that is recognized by both HVAC contractors and end market consumers. Scale advantages are realized throughout the organization and will strengthen further as Parts Plus stores are rolled out. The CEO has closely managed costs and allocated capital to the benefit of shareholders.

We sold our position in Edwards Lifesciences for several reasons. Firstly, while the transcatheter aortic valve replacement (TAVR) market continues to grow nicely, we are seeing more difficult comparisons, and therefore, a potential growth slowdown, as new TAVR center openings slow and procedure growth could be a major driver going forward. In addition, the competitive environment is getting more heated. While we believe Edwards can maintain share, pricing could be pressured going forward. Lastly, Edwards' mitral valve solution seems to be having even more delays in getting to trials.

### Outlook

We believe the stock market and business activity are off to a good start this year. Corrections in the equity market may occur at any time, but conditions for a more meaningful equity bear market do not seem to be in place. President Trump's policy agenda is becoming clearer than it was during the election. However, it is still too early to declare that we have all the details on his agenda for trade policies and foreign affairs. Our patience in not overreacting to last fall's Trump rally has been rewarded. We'll adjust our portfolios if Trump's actual initiatives become reality, rather than speculation or random proposals. From a stock selection perspective, we'll continue to focus on quality companies with protective moats that can do well in both good and bad economic times.

### Portfolio Highlights

**Style:** Mid Cap  
**Sub-Style:** Core  
**Index:** Russell Midcap<sup>®</sup>  
**Portfolio Inception:** 2000  
**Portfolio Assets:** \$340.8 M  
**Portfolio Turnover:** 25%–35%

### Investment Management Team

Name	Years of research experience
<b>Douglas S. Foreman, CFA</b> Chief Investment Officer	31
<b>Jon Christensen, CFA</b> Portfolio Manager + Senior Research Analyst	22
<b>Craig Stone</b> Portfolio Manager + Senior Research Analyst	28
<b>Todd Beiley, CFA</b> Senior Research Analyst	18
<b>Julie Kutasov</b> Senior Research Analyst	16
<b>Chris Wright, CFA</b> Senior Research Analyst	7
<b>Chris Benway, CFA</b> Research Analyst	8
<b>Julie Biel, CFA</b> Research Analyst	9

### Top Five Holdings

As of March 31, 2017

Company	Percent of equity (%)
Globus Medical	5.4
AMETEK	5.0
Bank of the Ozarks	4.4
Signature Bank	4.3
Skyworks Solutions	4.3
<b>Total</b>	<b>23.3</b>

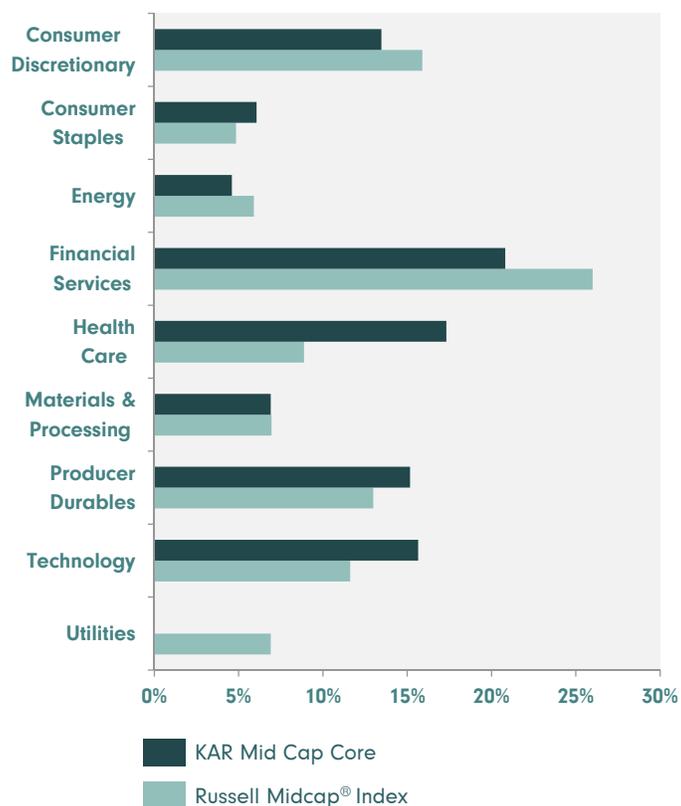
*This report is based on the assumptions and analysis made and believed to be reasonable by Advisor. However, no assurance can be given that Advisor's opinions or expectations will be correct. This report is intended for informational purposes only and should be not considered a recommendation or solicitation to purchase securities. A complete listing of portfolio holdings and specific security transactions for the preceding 12 months is available upon request. Holdings are subject to change. Holdings and weightings are based on a representative portfolio. Individual Investors' holdings may differ slightly. Data is obtained by FactSet Research Systems and is assumed to be reliable. Numbers may not always add up due to rounding. Past performance is no guarantee of future results.*

## Investment Process: Discovering Quality

Development of High-Quality Universe	Proprietary Fundamental Research	Portfolio Construction	Sell Discipline
<b>200 Stocks</b>  <b>Quantitative Screens</b> <ul style="list-style-type: none"> <li>High return on capital over a full economic cycle</li> <li>Long and resilient earnings history</li> <li>High return on net operating assets</li> <li>Minimal debt</li> </ul> <b>Other Resources</b> <ul style="list-style-type: none"> <li>Research on existing portfolio holdings</li> <li>Meetings with companies</li> <li>Industry reviews</li> <li>Investment conferences</li> <li>Third-party research</li> </ul>	<b>50–60 Stocks</b>  <b>Qualitative Analysis</b> <ul style="list-style-type: none"> <li>Evaluate sustainability of business model and assess management's ability to direct capital where it can create further control of its market</li> </ul> <b>Financial Analysis</b> <ul style="list-style-type: none"> <li>Evaluate basis for superior profitability, long-term growth potential, and ability to allocate capital appropriately</li> </ul> <b>Valuation Analysis</b> <ul style="list-style-type: none"> <li>Determine the current and potential value of the business</li> </ul>	<b>23–35 Stocks</b>  <b>Position Weights</b> <ul style="list-style-type: none"> <li>Average position size is typically 3%</li> <li>Max initial position size is 5% (cost)</li> <li>Max position size is 10% (market)</li> </ul> <b>Sector Tolerances</b> <ul style="list-style-type: none"> <li>+/- 10% of the sector weights of the Russell Midcap® Index</li> </ul> <b>Holding Period</b> <ul style="list-style-type: none"> <li>Typically 3-to-5 years</li> <li>Portfolio turnover is typically 25% to 35%</li> </ul> <b>Cash Levels</b> <ul style="list-style-type: none"> <li>Fully invested</li> <li>Max cash position is 10%</li> </ul>	<b>Extended Valuation</b>  <b>Portfolio Upgrade</b>  <b>Diversification Requirements</b>  <b>Acquisition Activity</b>  <b>Negative Company or Industry Changes</b>
Higher Quality   Stronger, More Consistent Growth   Better Value			

## Sector Diversification

As of March 31, 2017



A complete listing of portfolio holdings and specific security transactions for the preceding 12 months is available upon request. Holdings are subject to change. Holdings and weightings are based on a representative portfolio. Individual Investors' holdings may differ slightly. The sector information represented above is based on Russell sector classifications. Data is obtained by FactSet Research Systems and is assumed to be reliable.

## Portfolio Characteristics

As of March 31, 2017

	KAR Mid Cap Core	Russell Midcap® Index
<b>Quality</b>		
Return on Equity—Past 5 Years	25.9%	14.2%
Total Debt/EBITDA	1.9 x	3.9 x
Earnings Variance—Past 10 Years	31.5%	66.0%
S&P Stock Ranking (A+, A, A-, B+)	72.7%	44.3%
<b>Growth</b>		
Earnings Per Share Growth—Past 5 Years	11.2%	8.8%
Earnings Per Share Growth—Past 10 Years	13.4%	7.4%
Dividend Per Share Growth—Past 5 Years	14.1%	12.4%
Dividend Per Share Growth—Past 10 Years	17.3%	7.7%
Capital Generation—{ROE x (1-Payout)}	20.3%	9.6%
<b>Value</b>		
P/E Ratio—Trailing 12 Months	29.4 x	30.9 x
Dividend Yield	0.8%	1.7%
Free Cash Flow Yield†	4.1%	3.3%
<b>Market Characteristics</b>		
\$ Weighted Average Market Cap—4 Qtr. Avg.	\$11.3 B	\$13.2 B
Largest Market Cap—4 Qtr. Avg.	\$29.9 B	\$46.9 B
Annualized Standard Deviation—Since Inception*	14.1%	16.9%

\*January 1, 2000

†Free cash flow data is as of December 31, 2016. Prices are as of March 31, 2017. Excludes financials.

This material is deemed supplemental and complements the performance and disclosure at the end of this presentation. Data is obtained from FactSet Research Systems and BNY Mellon and is assumed to be reliable. Other principal consultant firms may use different algorithms to calculate selected statistics. Estimates are based on certain assumptions and historical information. Past performance is no guarantee of future results.

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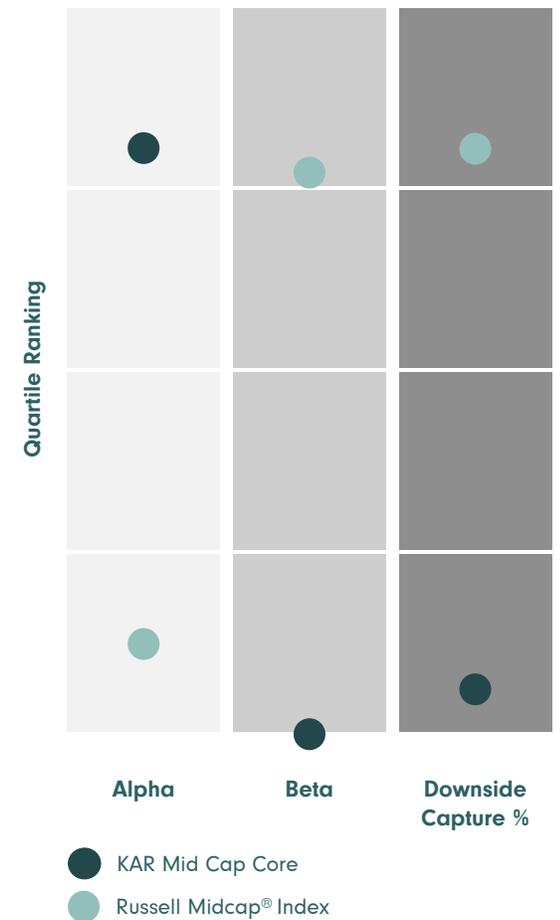
## Strong Risk-Adjusted Returns

Inception\* to March 31, 2017



## Peer Comparison Chart

Ten Years Ending March 31, 2017



## Historical Returns

	KAR Mid Cap Core (gross)	KAR Mid Cap Core (net) <sup>‡</sup>	Russell Midcap <sup>®</sup> Index
<b>Annualized Returns (%)<sup>†</sup></b>			
As of March 31, 2017			
1 <sup>st</sup> Quarter	5.75	5.56	5.15
One Year	15.43	14.58	17.03
Three Years	12.89	12.05	8.48
Five Years	14.14	13.30	13.09
Seven Years	14.30	13.43	13.15
Ten Years	9.28	8.37	7.94
Inception*	9.34	8.35	8.67
<b>Annual Returns (%)</b>			
2016	12.32	11.49	13.80
2015	3.37	2.60	(2.44)
2014	18.17	17.28	13.22
2013	28.54	27.62	34.76
2012	16.58	15.72	17.28
2011	4.52	3.76	(1.55)
2010	20.23	19.06	25.48
2009	21.11	19.92	40.48
2008	(28.63)	(29.37)	(41.46)
2007	6.45	5.40	5.60
2006	13.05	11.93	15.26
2005	8.86	7.78	12.65
2004	15.23	14.08	20.22
2003	26.72	25.49	40.06
2002	(12.62)	(13.50)	(16.19)
2001	(2.76)	(3.71)	(5.62)
2000	21.54	20.33	8.25

## Performance Statistics

Inception\* to March 31, 2017

	KAR Mid Cap Core	Russell Midcap <sup>®</sup> Index
Annualized Return	9.34	8.67
Annualized Standard Deviation	14.07	16.89
Alpha	2.10	0.00
Beta	0.76	1.00
Sharpe Ratio	0.55	0.41
R-Squared	84.38	100.00

\*January 1, 2000

<sup>†</sup>All periods less than one year are total returns and are not annualized. Returns are preliminary.

<sup>‡</sup>Net of all fees and expenses. Assumes a 0.75% annual fee.

This material is deemed supplemental and complements the performance and disclosure at the end of this presentation. Returns of the Kayne Anderson Rudnick composite are preliminary and gross of fees unless otherwise specified. For further details on the composite, please see the disclosure statement in this presentation. The Mid Cap Core Universe includes all managers categorized in the mid cap core asset class by eVestment. Data is obtained from FactSet Research Systems and is assumed to be reliable. Past performance is no guarantee of future results.

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### Disclosure

Kayne Anderson Rudnick 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. Kayne Anderson Rudnick Investment Management, LLC has been independently verified for the period from January 1, 1999 through December 31, 2014.

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. The Mid Cap Core Composite has been examined for the period from January 1, 2000 through December 31, 2014. The verification and performance examination reports are available upon request.

Kayne Anderson Rudnick Investment Management, LLC, a wholly owned subsidiary of Virtus Investment Partners, Ltd., is a registered investment advisor under the Investment Advisers Act of 1940. Registration of an Investment Advisor does not imply any level of skill or training. Kayne Anderson Rudnick Investment Management, LLC manages a variety of equity and fixed-income strategies focusing exclusively on securities the firm defines as high quality.

The composite includes all fully discretionary institutional and pooled Mid Cap Core Portfolios. Mid Cap Core Portfolios are invested in equity securities with market capitalizations consistent with the Russell Midcap® Index, that have market control, rising free cash flow, shareholder-oriented

management, strong consistent profit growth, and low-debt balance sheets. For comparison purposes, the composite is measured against the Russell Midcap® Index. The Russell Midcap® Index is a market capitalization-weighted index of the 800 smallest companies in the Russell 1000® Index, which comprises the 1,000 largest U.S. companies. The index is calculated on a total-return basis with dividends reinvested. Benchmark returns are not covered by the report of the independent verifiers. The composite was created in January 2000. As of January 1, 2011, the composite was redefined to include both institutional and mutual fund [or pooled] accounts. Previously, only institutional accounts were included. A list of composite descriptions and policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

Prior to January 1, 2011, the composite minimum was \$250,000. Prior to January 1, 2011, accounts that experienced a significant cash flow, defined as aggregate flows that exceeded 25% of the account's beginning of period market value, were temporarily removed from the composite.

The standard management fee schedule currently in effect is as follows: 0.75% for the first \$25 million; 0.65% on the next \$25 million; 0.55% on the next \$50 million; 0.50% on the balance. Actual management fees charged may vary depending on applicable fee schedules and portfolio size, among other things. Additional information may be found in Part 2A of Form ADV, which is available on request. The performance information is supplied for reference. Past performance is no guarantee of future results. Results will vary among accounts.

The U.S. dollar is the currency used to express performance. Returns are presented net of transaction fees and include the reinvestment of all income. Gross returns will be reduced by investment management fees and other expenses that may be incurred in the management of the account. Model net returns have been calculated by deducting 1/4th of the highest tier of the standard management fee schedule in effect for the respective period from the gross composite returns on a quarterly basis.

Internal dispersion is calculated using the asset-weighted standard deviation of annual gross returns for accounts in the composite for the entire year. For those years when less than five accounts were included for the full year, no dispersion measure is presented. The three-year annualized ex-post standard deviation measures the variability of the composite (using gross returns) and the benchmark for the 36-month period ended at the following dates:

3-Yr Annualized Standard Deviation (%)

December 31	Composite	Benchmark
2011	17.51	21.86
2012	15.39	17.44
2013	12.53	14.23
2014	10.29	10.29
2015	11.96	11.00

Year	Total Firm Assets (\$ millions)	Total Composite Assets (\$ millions)	Accounts at Year End	Gross Annual Return (%)	Net Annual Return (%)	Russell Midcap® Index Annual Return (%)	Internal Dispersion
2006	6,523	8	10	13.05	11.93	15.26	0.14
2007	5,392	7	8	6.45	5.40	5.60	0.19
2008	3,445	7	11	(28.63)	(29.37)	(41.46)	0.08
2009	4,010	8	9	21.11	19.92	40.48	0.40
2010	4,729	8	7	20.23	19.06	25.48	0.31
2011	5,232	10	14	4.52	3.76	(1.55)	0.26
2012	6,545	11	15	16.58	15.72	17.28	0.18
2013	7,841	15	15	28.54	27.62	34.76	0.48
2014	7,989	17	12	18.17	17.28	13.22	0.13
2015	8,095	42	16	3.37	2.60	(2.44)	0.44

The Russell Midcap® Index is a trademark/service mark of Frank Russell Company. Russell® is a trademark of Frank Russell Company.