

## Small-Mid Cap Quality Value Portfolio

Fourth Quarter 2016



### Portfolio Review

The Small-Mid Cap Quality Value portfolio lagged the Russell 2500 Value Index during the fourth quarter. The underperformance was primarily driven by negative stock selection and an underweight to the financial services sector, in addition to negative stock selection in the technology sector. Performance was helped by strong stock selection in the consumer discretionary, and the materials and processing sectors.

Positions that contributed most positively to performance during the quarter were Cass Information Systems and Bank of Hawaii. Cass Information Systems' shares rose sharply following the presidential election, driven by investor expectations of rising short-term interest rates, higher fuel prices and meaningful economic stimulus through tax reform, infrastructure spending and deregulation.

Bank of Hawaii has generated return-on-equity well above most mainland U.S. banks. Its most recent quarter's results were slightly better-than-expectations. However, the shares had been under some pressure as the prospect for additional rate hikes by the U.S. Federal Reserve had diminished. However, with the Trump administration expected to drastically reduce federal regulation and the pace of Fed rate increases to accelerate, those concerns have been pushed aside.

Positions that contributed most negatively to performance during the quarter were Syntel and Patterson Companies. Syntel again reported weak results, with sluggish end-market demand. Management commented that decision cycles continue to lengthen with persistent contract delays. Customer concentration has been an ongoing issue for the company and is a concern from the standpoint of long-term prospects and profitability.

Patterson's shares exhibited weakness in the quarter after the company announced it was terminating its exclusive distribution agreement with Dentsply Sirona. With the solid organic growth that Denstply has seen, this creates a large unknown in Patterson's future revenue flow.

### Purchases and Sales

In the Small-Mid Cap Quality Value portfolio, we purchased Axalta Coating Systems, TransUnion and W.R. Berkley Corporation. We also sold our position in Syntel, Village Supermarket, RLI Corp and Ross Stores.

Axalta Coating Systems manufactures paint and coating systems for vehicle and industrial applications. Axalta's scale enables painter and process training; helps provide the ability to run Original Equipment Manufacturer (OEM) painting operations at the OE's facilities, and facilitates global offerings to OEMs.

TransUnion holds a dominant position in the market for consumer credit reporting—an attractive industry characterized by high barriers-to-entry due to significant database infrastructure, technology and maintenance costs. TransUnion's strong recurring revenue stream, coupled with a stable customer base provides the company with a solid defensible position.

W.R. Berkley is a specialty lines commercial property and casualty insurance company. It has a strong underwriting culture that is focused on generating operating profits through a full cycle (10 years), and not premium volume targets. Operations are largely decentralized, with decisions pushed down to the operating units and front-line underwriters, but supported by resources (e.g. actuarial, etc.) and subject to regular oversight at the corporate level.

Syntel's competitive position is deteriorating and attrition continues as it moves to automate more core job functions. Moreover, its market opportunity remains uncertain as technology and automation continue to grow, and core maintenance companies are willing to spend on contracts. Coupled with material turnover in senior management over the last couple of years, the recapitalization of its balance sheet, the assumption of additional debt after paying out an exorbitant special dividend from expatriated cash, further lends to our decision to sell our holding.

Village Supermarket is being challenged by the intensifying competitiveness of the industry, resulting in gross margin pressure and the need to make additional capital investments to maintain consumer traffic. Given that the company's previous expansion plans into Baltimore was not a success, we are skeptical that moving into a competitive market like the Bronx can be different than last foray outside the company's core New Jersey market just because it is closer geographically.

We also sold our position in RLI to purchase another insurance company, W. R. Berkley, which has more compelling long-term valuation.

Additionally, we sold the balance of our Ross Stores holding due to market capitalization. We are utilizing the proceeds to help fund a new purchase that is smaller in market capitalization that we believe will have better long-term return potential.

### Outlook

As we peer into 2017, we believe there is more than a usual amount of economic uncertainty. President-elect Trump has no public office track record for us to assess and judge how effective he will be in getting changes accomplished. It does seem highly likely that some form of corporate and personal tax reform, partial ACA repeal, increased infrastructure spending and less regulatory burden for many businesses will occur over the next two years. However, the timing of these changes are unclear. If these events were to occur, we believe the economy should accelerate and grow in the 2.5% to 3.5% range for the next couple of years. We also believe that the S&P 500 earnings-per-share growth should pick up from the low single-digit range to the mid-to-high single-digit growth range as economic growth increases over the next year.

## Portfolio Highlights

**Style:** Small-Mid Cap  
**Sub-Style:** Value  
**Index:** Russell 2500™ Value  
**Portfolio Inception:** 2008  
**Portfolio Assets:** \$424.1 M  
**Portfolio Turnover:** 25%–35%

## Investment Management Team

Name	Years of research experience
<b>Douglas S. Foreman, CFA</b> Chief Investment Officer	30
<b>Julie Kutsov</b> Portfolio Manager + Senior Research Analyst	15
<b>Craig Stone</b> Portfolio Manager + Senior Research Analyst	27
<b>Todd Beiley, CFA</b> Senior Research Analyst	17
<b>Jon Christensen, CFA</b> Senior Research Analyst	21
<b>Chris Wright, CFA</b> Senior Research Analyst	6
<b>Chris Benway, CFA</b> Research Analyst	7
<b>Julie Biel, CFA</b> Research Analyst	8

## Top Five Holdings

As of December 31, 2016

Company	Percent of equity (%)
Cass Information Systems	4.5
RBC Bearings	4.4
Cheesecake Factory	4.3
Cinemark Holdings	4.1
Graco	3.7
<b>Total</b>	<b>21.0</b>

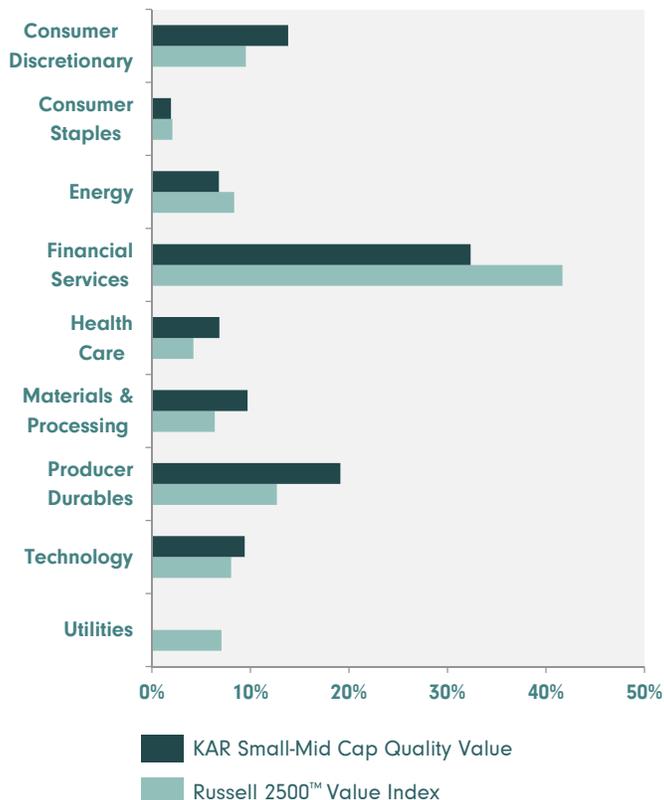
*This report is based on the assumptions and analysis made and believed to be reasonable by Advisor. However, no assurance can be given that Advisor's opinions or expectations will be correct. This report is intended for informational purposes only and should be not considered a recommendation or solicitation 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. 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 2500™ Value 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 December 31, 2016



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 December 31, 2016

	KAR Small-Mid Cap Quality Value	Russell 2500™ Value Index
<b>Quality</b>		
Return on Equity—Past 5 Years	21.0%	8.7%
Total Debt/EBITDA	1.7 x	5.9 x
Earnings Variance—Past 10 Years	24.5%	87.6%
S&P Stock Ranking (A+, A, A-, B+)	74.5%	24.1%
<b>Growth</b>		
Earnings Per Share Growth—Past 5 Years	10.6%	8.1%
Earnings Per Share Growth—Past 10 Years	8.3%	5.0%
Dividend Per Share Growth—Past 5 Years	15.4%	10.0%
Dividend Per Share Growth—Past 10 Years	12.5%	3.1%
Capital Generation—{ROE x (1-Payout)}	12.9%	5.9%
<b>Value</b>		
P/E Ratio—Trailing 12 Months	23.4 x	28.5 x
Dividend Yield	1.7%	2.0%
Free Cash Flow Yield†	4.8%	3.1%
<b>Market Characteristics</b>		
\$ Weighted Average Market Cap—4 Qtr. Avg.	\$5.3 B	\$3.9 B
Largest Market Cap—4 Qtr. Avg.	\$21.7 B	\$13.5 B
Annualized Standard Deviation—Since Inception*	17.0%	19.5%

\*January 1, 2008

†Free cash flow data is as of September 30, 2016. Prices are as of December 31, 2016.

Excludes financials.

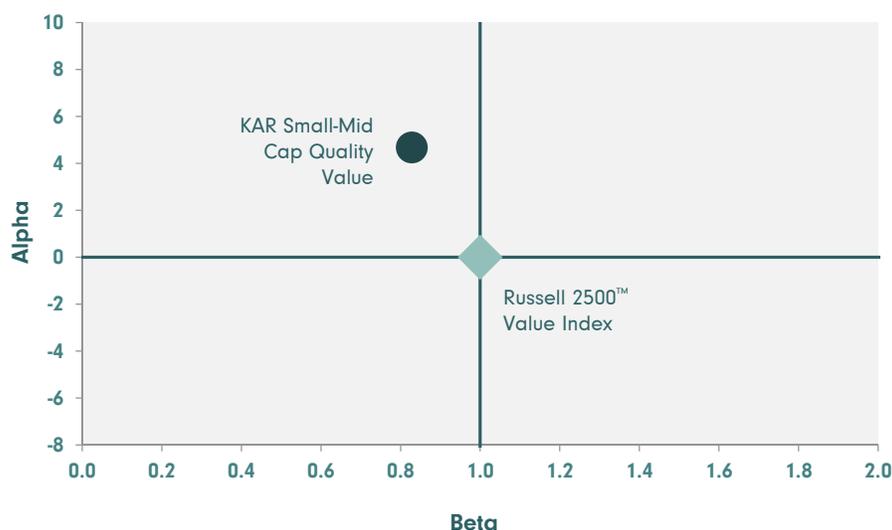
This material is deemed supplemental and complements the performance and disclosure at the end of this presentation. Data is obtained from FactSet Research Systems and BNY Mellon and is assumed to be reliable. Other principal consultant firms may use different algorithms to calculate selected statistics.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

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Fourth Quarter 2016

## Risk-Return Analysis

Inception\* to December 31, 2016



## Peer Comparison Chart

Inception\* to December 31, 2016



## Historical Returns

	KAR Small-Mid Cap Quality Value (gross)	KAR Small-Mid Cap Quality Value (net) <sup>†</sup>	Russell 2500 <sup>™</sup> Value Index
<b>Annualized Returns (%)<sup>†</sup></b>			
As of December 31, 2016			
4 <sup>th</sup> Quarter	6.82	6.58	9.34
One Year	19.69	18.63	25.20
Three Years	9.02	8.04	8.22
Five Years	14.41	13.40	15.04
Seven Years	14.93	13.92	13.52
Inception*	12.31	11.29	8.65
<b>Annual Returns (%)</b>			
2016	19.69	18.63	25.20
2015	(0.58)	(1.47)	(5.49)
2014	8.88	7.89	7.11
2013	36.30	35.12	33.32
2012	11.01	10.07	19.21
2011	7.40	6.52	(3.36)
2010	25.83	24.61	24.82
2009	32.52	31.23	27.68
2008	(19.00)	(19.84)	(31.99)

## Performance Statistics

Inception\* to December 31, 2016

	KAR Small-Mid Cap Quality Value	Russell 2500 <sup>™</sup> Value Index
Annualized Return	12.31	8.65
Annualized Standard Deviation	17.01	19.51
Alpha	4.67	0.00
Beta	0.83	1.00
Sharpe Ratio	0.71	0.43
R-Squared	90.15	100.00

\*January 1, 2008

<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 0.90% 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 Small-Mid Cap Value Universe includes all managers categorized in the small-mid cap value 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

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 Small-Mid Cap Quality Value Composite has been examined for the period from January 1, 2012 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 is defined as all fully discretionary institutional and pooled Small-Mid Cap Quality Value Portfolios (including cash) under management for at least one full quarter. Small-Mid Cap Quality Value Portfolios are invested in equity securities with market capitalizations consistent with the Russell 2500™ Value 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 2500™ Value Index. The Russell

2500™ Value Index is a market capitalization-weighted index of value-oriented stocks of the 2,500 smallest companies in the Russell Universe, which comprises the 3,000 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 June 2008. 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. 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. This composite contained 0.16% non-fee-paying portfolios as of December 31, 2013 and 0.2% non-fee-paying portfolios as of December 31, 2014.

The standard fee schedule in effect is as follows: 0.90% for the first \$25 million; 0.80% on the next \$25 million; 0.75% on the next \$50 million; 0.60% 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 IIA 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 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		20.08	24.57
2012		13.97	18.67
2013		12.01	15.29
2014		10.66	11.41
2015		12.25	12.19

Year	Total Firm Assets (\$ millions)	Total Composite Assets (\$ millions)	Accounts at Year End	Gross Annual Return (%)	Net Annual Return (%)	Russell 2500™ Value Index Annual Return (%)	Internal Dispersion
2008	3,445	< 1	< 5	(19.00)	(19.84)	(31.99)	N/A
2009	4,010	< 1	< 5	32.52	31.23	27.68	N/A
2010	4,729	< 1	< 5	25.83	24.61	24.82	N/A
2011	5,232	1	< 5	7.40	6.52	(3.36)	N/A
2012	6,545	85	< 5	11.01	10.07	19.21	N/A
2013	7,841	138	6	36.30	35.12	33.32	0.13
2014	7,989	140	12	8.88	7.89	7.11	0.09
2015	8,095	371	17	(0.58)	(1.47)	(5.49)	0.05

The Russell 2500™ Value Index is a trademark/service mark of Frank Russell Company. Russell® is a trademark of Frank Russell Company.