Market Review Commentary

August 2021

Kayne Anderson Rudnick Investment Management

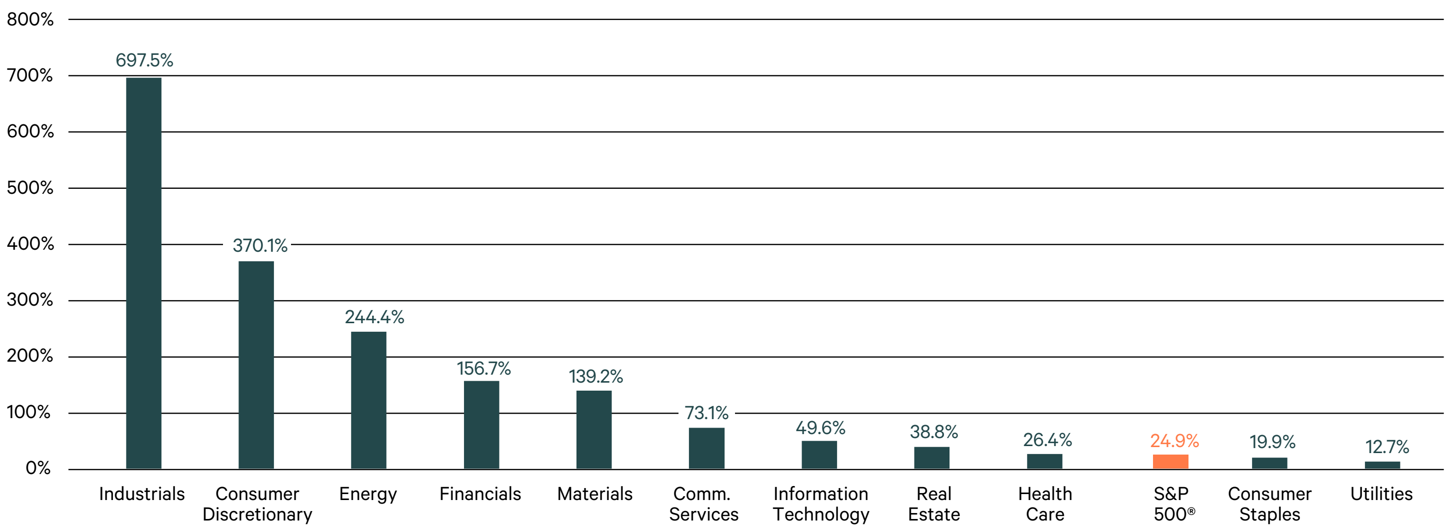
August historically has not been a kind month to equity returns, but that trend was not borne out this year. With concerns such as Federal Reserve tapering, the debt ceiling, inflation fears, a new infrastructure bill, potential higher taxes, the Delta variant, and the U.S. withdrawal from Afghanistan—there was no shortage of potential market pitfalls, yet the S&P 500 Index continued to record new highs and the 10-Year Treasury ended the month at 1.30%, a decline from its April month-end peak of 1.64%.

So why has the market continued to do so well? Two things help explain the market's upward move—interest rates and corporate earnings. Interest rates are benign with the 30-year bond below the Fed's long-term target of 2.0% and, as discussed earlier, the 10-Year Treasury has declined from its peak. Inflation is up due to supply constraints in a variety of industries and increasing energy prices. However, we believe that what we are experiencing is transitory inflation, or temporary price increases, as the Fed projected in its many public statements. As supply chain gridlock continues to loosen up, we believe inflation concerns will in fact prove to be temporary.

Even in a COVID-19 constrained environment, second quarter corporate earnings soared across many sectors and industries. In fact, the second quarter marked the highest year-over-year earnings growth reported by the S&P 500 Index since the fourth quarter of 2009.

FIGURE 1: S&P 500® 2Q 2021 ESTIMATED EARNINGS GROWTH RATE

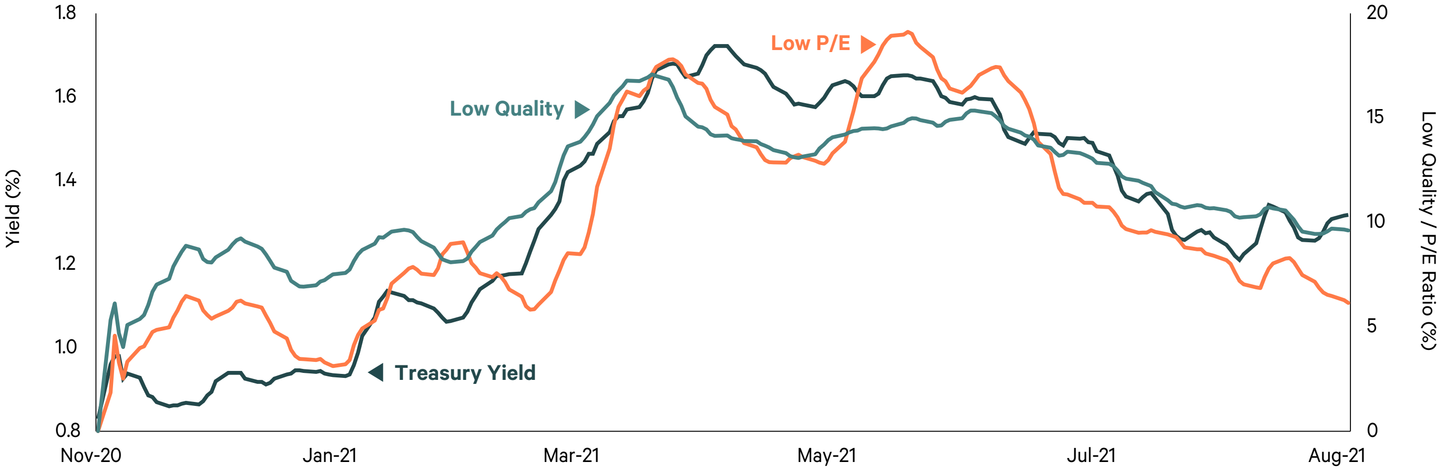
Quarterly Year-Over-Year Percent Change



Data presented is as of September 3, 2021. Data is obtained from Strategas and is assumed to be reliable. ***Past performance is no guarantee of future results.***

The market also rotated back in favor of quality companies that have stable earnings during the beginning months of the third quarter. This is a reversal from the fourth quarter 2020 and the first quarter 2021, where low quality companies outperformed and were the early beneficiaries of the economic reopening. As the reopening progressed during the second quarter, both low and high quality companies performed in line. So far in the third quarter (as of the end of August), quality companies have regained the market's favor. We noted in the second quarter that it will be interesting to see over the remainder of the year if indeed low quality has already run its course.

FIGURE 2: 10-YEAR TREASURY YIELDS VS. QUALITY AND VALUE FACTORS



When Treasury yields and credit spreads diverged on March 31, the S&P 500 Index followed the path of spreads. More specifically, low Valuation and low Quality stocks outperformed from Pfizer's vaccine announcement (November 9, 2020) through the peak in 10-Year yields (March 31, 2021) and have lagged since. Data is presented as of August 31, 2021. Data is obtained from Credit Suisse Securities (USA) LLC and is assumed to be reliable. ***Past performance is no guarantee of future results.***

Despite where the low quality vs. high quality metrics may lead, KAR will continue to purchase high quality businesses for its clients regardless of market and economic events. We believe competitive protections and differentiation are the key investment metrics that matter the most over the long term.

We thank you for your continued trust and confidence in managing your assets.

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Douglas S. Foreman, CFA is Chief Investment Officer, Portfolio Manager, and a member of the Executive Management Committee. He has approximately 35 years of investment experience.

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