Market Review Commentary

Second Quarter 2023

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MARKET PERFORMANCE

After an extremely difficult year for stocks and bonds in 2022, U.S. equities continued to climb in the second quarter with the S&P 500 advancing a solid 8.74%, bringing the year-to-date return up to 16.89%. Large-capitalization growth stocks, as measured by the Russell 1000 Growth Index, have been the best performers by far advancing 12.81% for the quarter and 29.02% for the year-to-date. Market breadth continued to be mediocre with the Russell 1000 Value Index up 4.07% for the quarter and 5.12% for the year-to-date.

FIGURE 1: CONTRIBUTION OF 10 LARGEST WEIGHTS IN THE S&P 500® TO ANNUAL RETURNS DURING POSITIVE PERFORMANCE YEARS

Year	Top 10 % of Return	S&P 500® Performance
2023 YTD	85.8%	12.7%
2007	78.7%	3.5%
2020	58.9%	16.3%
1999	54.5%	19.5%
2021	45.0%	26.9%
1998	36.8%	26.7%
1996	33.9%	20.3%
2017	33.3%	19.4%
2019	32.8%	28.9%
1991	28.6%	26.3%
2006	27.6%	13.6%
2016	26.6%	9.5%
2003	23.6%	26.4%
1995	22.3%	34.1%
2014	22.2%	11.4%
2004	21.1%	9.0%
2005	20.5%	3.0%
2010	19.6%	12.8%
2012	19.2%	13.4%
1997	19.1%	31.0%
2013	17.6%	29.6%
2009	15.5%	23.5%
1992	14.9%	4.5%
1993	12.2%	7.1%

Data is obtained from Strategas and is assumed to be reliable. Year-to-date data as of June 27, 2023. Performance presented is for the S&P 500 Price Index. ***Past performance is no guarantee of future results.***

Small-capitalization stocks, as measured by the Russell 2000 Index, advanced 5.21% in the quarter and 8.09% for the year-to-date. International equities, as measured by the MSCI EAFE Index, only advanced 2.95% in the quarter but they have returned 11.67% for the year-to-date. The MSCI Emerging Markets Index was a laggard advancing 0.90% for the quarter and 4.89% for the year-to-date.

During the quarter, the 10-year U.S. Treasury yield backed up slightly from 3.49% to 3.81%. This resulted in the Bloomberg U.S. Aggregate Bond Index declining 0.84% for the quarter, although it is still positive for the year-to-date returning 2.09%. High-yield bonds, as measured by the ICE BofA U.S. High Yield Index, fared better advancing 1.63% for the quarter, bringing the year-to-date return to 5.42%. Municipal bonds, as measured by the Bloomberg U.S. Municipal Bond Index, were down slightly for the quarter declining 0.10%, but positive for the year-to-date returning 2.67%.

WHY HAVE THE BIG SEVEN TECH STOCKS PERFORMED SO WELL?

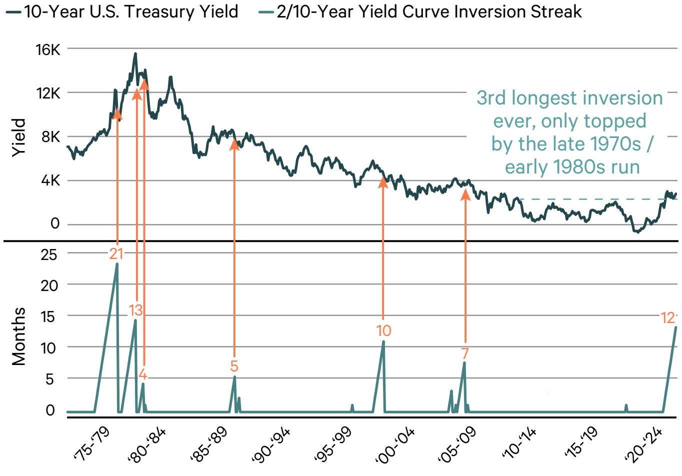
It is clear that market returns this quarter, particularly in the S&P 500 and Russell 1000 Growth benchmarks, were concentrated in the largest technology stocks. This list includes Apple, Microsoft, Amazon, Meta, NVIDIA, Tesla, and Alphabet. These companies were hit hard in last year's bear market and had been cost cutting late last year to right-size their businesses.

Artificial intelligence (AI) interest started to pick up in the first quarter of 2023 and most analysts and investors believed it would take years for this transformational technology to have a meaningful impact on many businesses. Skeptical AI critics were then hit with NVIDIA's first quarter earnings report which indicated an enormous pickup in AI chip spending during the second quarter. Accenture, a leading system integration company, announced a $3 billion investment into developing their AI practice as well. The reason these behemoths have benefited initially is that they have enormous amounts of data to work with as well as robust balance sheets which will allow them to fund the necessary investments to exploit this exciting new technology. So, while the promise of AI has positively impacted the larger companies initially, over time it will impact every industry positively or negatively—very similar to the birth of the internet in the 1990s or the development of the cloud over the last decade. Our job as active managers at KAR will be to seek out those companies that have competitive advantages as this technology is deployed over time.

WHAT COULD IMPROVE MARKET BREADTH FROM HERE?

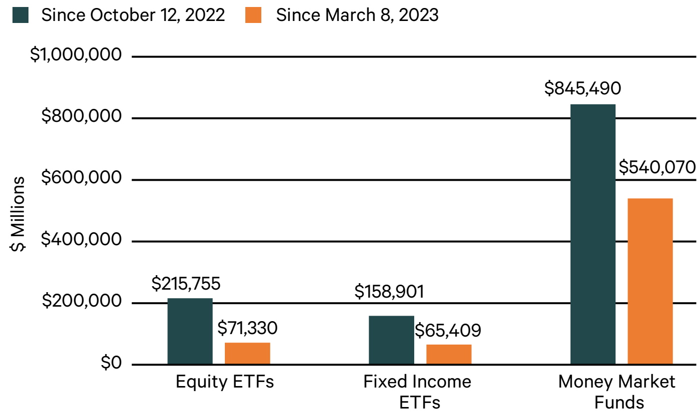
Smaller companies and the other 493 stocks of the S&P 500 have been relative laggards since the market bottomed last October. We believe the principal reason this is happening is the inverted yield curve. The curve has continued to be inverted leading investors to fear an impending recession (which has yet to materialize) and a lackluster GDP environment which is not friendly to many cyclically sensitive industries. We believe the yield curve needs to start to flatten out and ultimately resume its normal positive slope for the market to see sustainable improvements in market breadth.

FIGURE 2: 2/10-YEAR YIELD CURVE INVERSION NOW IN 12TH CONSECUTIVE MONTH



Data presented is as of June 12, 2023, is obtained from Strategas and is assumed to be reliable. ***Past performance is no guarantee of future results.***

FIGURE 3: FUND FLOWS–EQUITY ETFS VS. FIXED INCOME ETFS VS. MONEY MARKET FUNDS



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ANOTHER BANKING CRISIS?

Continued improvements in the Fed's fight against inflation will be needed to at least flatten the curve. Fortunately, the inflation data continues to trend lower and we believe that this seems likely to continue over the next 12 to 18 months. In our view, this can set the stage for little to no further short-term interest rate increases from here. If you exclude the P/E ratios of the top 7 companies in the S&P 500 Index, valuations decline to the 13-to-17x earnings for the rest of the market. This valuation backdrop can help offset any mild decline in earnings even if the economy does slip into a mild or shallow recession. We have seen some improvements in breadth over the last half of this quarter, but not robust enough yet to call it a trend. If breadth expands, this would be a positive sign for equities.

WHAT ARE INVESTORS DOING IN THE MARKETS?

Investors are seeking the comfort of cash after the difficult year in 2022 for both stocks and bonds, which is temporarily earning 5% in many money market funds.

This is completely understandable given recent investor experience and an uncertain economic outlook. However, we believe this is likely to be a temporary solution for many investors if the Fed continues to be successful in its inflation fight. Investors in cash will be faced with declining yields probably accompanied with an improving equity market, making it difficult to time a good re-entry point. From our perspective, staying focused on long-term goals and allocations will probably yield better long-term results than hoarding cash at this point.

As always, thank you for your trust and confidence in managing your assets. We will continue to own what we believe are quality businesses with a competitive moat that will protect their economics.

Douglas S. Foreman, CFA
Chief Investment Officer

Douglas S. Foreman, CFA is Chief Investment Officer, Portfolio Manager, and a member of the Executive Management Committee. He has approximately 37 years of investment experience.

Large-capitalization stocks are represented by the S&P 500® Index which is a market capitalization weighted index which includes 500 of the largest companies in leading industries of the U.S. economy. Growth stocks are represented by the Russell 1000® Growth Index which is a market capitalization-weighted index of growth-oriented stocks of the 1,000 largest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Value stocks are represented by the Russell 1000® Value Index which is a market capitalization-weighted index of value-oriented stocks of the 1,000 largest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Small-capitalization stocks are represented by the Russell 2000® Index which is a market capitalization-weighted index of the 2,000 smallest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Emerging markets are represented by the MSCI® Emerging Markets (EM) Index which is a free float-adjusted market capitalization index tracking the equity performance of global emerging markets. The Bloomberg U.S. Aggregate Bond Index is a market value weighted index that tracks the daily price, coupon, pay downs and total return performance of fixed-rate, publicly placed, dollar-denominated and non-convertible investment grade debt issues with at least $250 million par amount outstanding with at least one year to final maturity. Performance is calculated on a total return basis with dividends reinvested. The MSCI® EAFE Index is a free float-adjusted market capitalization index that measures developed foreign market equity performance, excluding the U.S. and Canada. The Bloomberg U.S. Municipal Index covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prefunded bonds. The ICE BofAML U.S. High Yield Index tracks the performance of U.S. dollar denominated below-investment-grade corporate debt publicly issued in the U.S. domestic market. 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 not be considered a recommendation or solicitation to purchase securities. ***Past performance is no guarantee of future results.***