Small/Mid Cap Equity

1Q 2021 Commentary

Small/Mid Cap Rally Continues, Leading to Near-Record 12-Month Return

Small/mid cap equities continued to generate robust positive returns in the first quarter of 2021, as the Russell 2500 Index returned 10.93% for the period. While short squeezes had an outsized effect on small cap returns earlier in the quarter (to the dismay of many active managers), the dominant factors that boosted equity prices throughout the period included optimism surrounding the COVID-19 vaccine and a hefty fiscal stimulus package adopted by Congress. Treasury yields rose meaningfully during the quarter (a continuation from the fourth quarter of 2020) with the 10-year yield rising from 0.93% at year-end to 1.74% on March 31, on expectations that increased fiscal stimulus could lead to faster economic growth and higher inflation. Rising rates and a steeper yield curve benefited cyclical, value-oriented segments of the market in the first quarter, as these areas are generally expected to do well in a reflationary environment.

Overall, the pace of the rally over the last year has been nothing short of astounding, with the Russell 2500 Index generating a cumulative total return of 120.91% since the small/mid cap market bottomed on March 23, 2020, compared to "just" 85.86% for the large cap Russell 1000 Index. For the one-year period ending March 31, 2021, the Russell 2500 Index returned 89.40%, the second-highest output for the small/mid cap market in a one-year period (using month- or quarter-end data) since the benchmark's inception. Despite the near-record performance for small/mid cap equities over this time, history would suggest that forward returns can remain positive going forward. In fact, the Russell 2500 Index has generally produced a strong return in the three-year period following similarly strong rallies, as shown in the table below listing the ten best one-year periods since the benchmark's inception (excluding the first quarter) and their subsequent returns. While history does not always repeat itself, we believe the small/mid cap market continues to provide attractive upside potential, especially for companies with strong fundamentals and reasonable valuations.

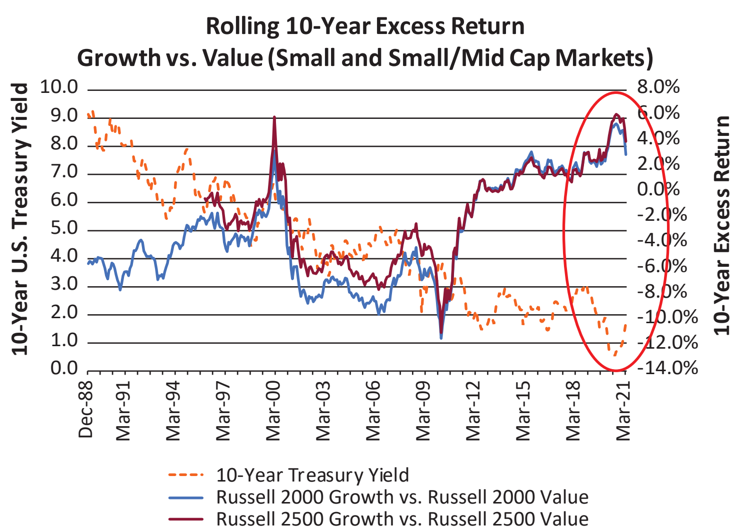
Small/Mid Cap Market		
1-Year Ending	Russell 2500 Index Return	Subsequent 3-Year Annualized Return
June 1983	90.18	13.42
March 1981	66.02	12.33
March 2010	65.71	14.59
September 1983	64.62	10.67
March 2004	60.64	13.26
March 1983	60.48	17.25
September 1991	46.83	13.87
December 1991	46.70	10.24
December 2003	45.51	14.10
March 2000	43.48	-1.36

Source: eVestment

Cyclical, Value-Led Rally in the First Quarter

Every sector in the Russell 2500 Index with the exception of Health Care advanced during the quarter. As previously mentioned, we believe the rising rate environment provided a favorable backdrop for more cyclical, value-oriented securities, with Energy (38.02%*), Consumer Discretionary (21.38%*), Financials (18.66%*) and Industrials (15.10%*) leading the way during the period. The Materials (14.44%*) and Consumer Staples (12.96%*) sectors also contributed positively, outperforming the broader small/mid cap market. Health Care (-0.17%*), Information Technology (1.25%*) and Utilities (3.20%*) were the weakest sectors in the first quarter, while Communication Services (8.85%*) and Real Estate (9.98%*) also underperformed despite generating strong absolute returns.

From a style perspective, the Russell 2500 Value Index outperformed the Russell 2500 Growth Index for a second consecutive quarter, with a respective total return of 16.83% versus 2.49% in the first quarter. Much of this outperformance was driven by the sector leadership discussed in the previous paragraph, as these sectors generally have a higher representation in the small/mid cap value benchmark. We have discussed the strong relative performance of longer-duration equities in previous iterations of this commentary. These securities, which are typically described as "growth stocks" given much of their perceived value is derived from future cash flows that may not be realized for a number of years, have outperformed meaningfully since Treasury yields began declining in 2018. While longer-duration assets may promise higher growth in the future, they are also generally more sensitive to movements in interest rates. As expected, longer-duration assets such as those found in the biotechnology and software sectors underperformed in the first quarter given the upward pressure on rates, which has a direct impact on a company's discount rate.



Source: FactSet
Past performance is not indicative of future results. Please see important disclosures at the end of this document.

*Percentage represents index sector return for the quarter.

Despite value's recent outperformance, the trailing 10-year relative performance between growth and value (depicted in the chart below), which eclipsed the extremes of the dot-com bubble in 2020, suggests further normalization will likely occur to the benefit of value-oriented investors. As such, we believe the current environment and the market's reflationary expectations may continue to pressure these longer-duration businesses, which could provide a more favorable backdrop for companies with strong free cash flow characteristics and lower valuations going forward.

Mixed Bag for Quality Factors

While value recaptured a portion of its multi-year underperformance in the first quarter, it was more of a mixed bag for quality. In a welcome change from 2020, companies with positive earnings generally outperformed loss-makers during the period. However, companies with low returns on equity, greater earnings variability, higher leverage and higher betas also outperformed. We believe this is an important factor going forward, especially on the heels of the strong one-year period for the small/mid cap market. While valuation expansion typically drives stock market returns in the early stages of a recovery (as was the case in the last nine months of 2020), later gains are typically driven by earnings growth. We believe this should benefit companies with stronger earnings profiles and less earnings variability going forward.

Performance Review

For the first quarter of 2021, the Aristotle Small/Mid Cap Equity Composite generated a total return of 9.76% gross of fees (9.65% net of fees) compared to the 10.93% total return of the Russell 2500 Index. Sector allocation was the primary detractor during the quarter, followed by security selection. Security selection within the Information Technology, Health Care and Utilities sectors added the most value on a relative basis, while the Industrials, Consumer Staples and Real Estate sectors were the largest detractors. From an allocation perspective, the portfolio benefited from overweights in Financials and Industrials; however, this was offset by an underweight in Consumer Discretionary and an overweight in Information Technology.

The entirety of the Small/Mid Cap Equity Composite's underperformance came in the first half of the quarter, as the portfolio's underexposure to the most heavily shorted companies in the benchmark detracted during the small cap short-squeeze rally to begin the year. As this noise cleared and the market shifted towards rewarding companies with more attractive valuations, we were pleased to see the portfolio outperform the Russell 2500 Index meaningfully from the middle of February to the end of the quarter.

Relative Contributors	Relative Detractors
Signature Bank	Bottomline Technologies
Pacific Premier Bancorp	Chemed
Designer Brands	Itron
BankUnited	Cohen & Steers
PacWest Bancorp	Carter's

CONTRIBUTORS

Security selection added the most value within the Information Technology, Health Care and Utilities sectors. Additionally, overweights in Financials and Industrials contributed positively to relative performance. At the company level, **Signature Bank** and **Pacific Premier Bancorp** were two of the largest contributors during the quarter.

- **Signature Bank (SBNY)**, a full-service commercial bank with offices in New York, California and North Carolina, benefited from strong balance sheet growth and strong performance in its digital payments platform. We maintain a position, as we believe the company's differentiated business model and investments in end markets, such as fund banking and digital asset solutions, should drive attractive growth relative to peers and create value for shareholders.

- **Pacific Premier Bancorp (PPBI)**, a California-based bank holding company primarily focused on serving small and middle market businesses, benefited from strong trends in its core fee business as well as higher net interest income. We maintain a position, as we believe the company's strong balance sheet, lending pipeline and ability to expand its fee income business should create additional value for shareholders.

DETRACTORS

Security selection detracted within the Industrials, Consumer Staples and Real Estate sectors. Additionally, the portfolio's underweight in Consumer Discretionary and overweight in Information Technology detracted from relative performance. At the company level, **Bottomline Technologies** and **Chemed** were two of the largest detractors during the quarter.

- **Bottomline Technologies (EPAY)**, a financial technology business that provides cloud-based settlement networks on a software-as-a-service basis, declined following a mixed earnings report that included lower-than-expected subscription and transaction revenues. We maintain a position, as we believe the company's differentiated products and services, including an industry-leading business-to-business payment platform, along with management's efforts to increase subscription growth will create shareholder value going forward.

- **Chemed Corporation (CHE)**, a holding company that engages in the provision of healthcare and maintenance services through two distinct subsidiaries, was negatively impacted during the quarter by uncertainty regarding occupancy referral volume for its hospice business. We maintain a position, as we believe the strong long-term demand in both of the company's core businesses will lead to attractive growth and value creation for shareholders.

Recent Portfolio Activity

Buys/Acquisitions	Sells/Liquidations
Box	RPC
Diamondback Energy	QEP Resources
eHealth	

BUYS/ACQUISITIONS

- **Box, Inc. (BOX)**, a technology company focused on cloud content management and file-sharing services for businesses, was added to the portfolio. We believe Box's leading cloud content management platform provides significant opportunity for the business to take share as more companies shift content management to the cloud and away from on-premises vendors.
- **Diamondback Energy, Inc. (FANG)**, an independent oil and natural gas company focused on the acquisition, development and exploration of unconventional and onshore oil and gas reserves, was added to the portfolio following the company's acquisition of portfolio holding QEP Resources.
- **eHealth, Inc. (EHTH)**, an online broker of Medicare, individual/family, small business and ancillary insurance products, was added to the portfolio. We believe the company is well-positioned to benefit from expanding Medicare enrollment trends and its leading position as an omnichannel broker should allow the company to increase its market share as online enrollment and services continue to expand.

SELLS/LIQUIDATIONS

- **RPC, Inc. (RES)**, an oilfield services company primarily focused on the completion phase of well development in the United States, was removed from the portfolio due to concerns that the company's earnings power could be hampered by increasing competitive pressure in the industry.
- **QEP Resources, Inc. (QEP)**, an independent natural gas, oil exploration and production company was removed from the portfolio by virtue of being acquired by Diamondback Energy.

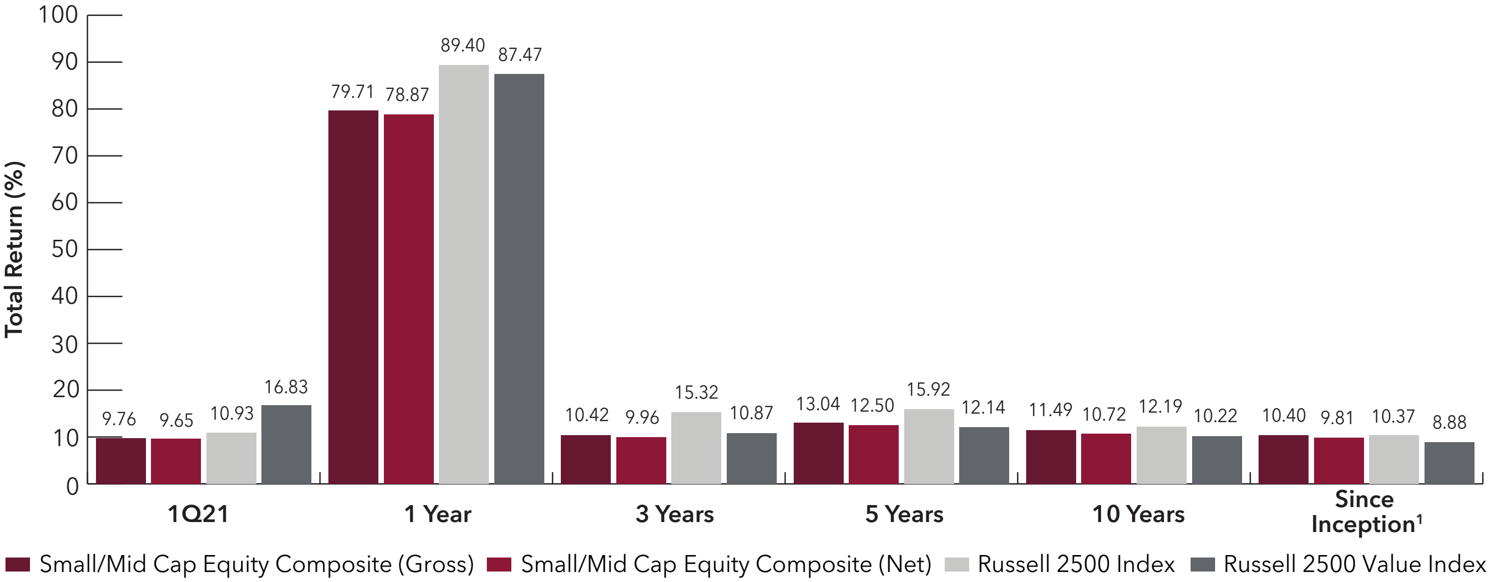
Outlook and Positioning

Our long-term outlook for the small/mid cap equity market remains positive, and we believe the current environment should provide a favorable backdrop for companies with strong fundamentals and attractive valuations over the next multi-year period. The pandemic environment that drove the markets last year created a headwind for many cyclical areas of the market, leading to a favorable environment for longer-duration growth companies and significant outperformance of money-losing companies relative to profitable businesses. We believe our focus on businesses with strong fundamentals and attractive valuations will be rewarded as these relative performance relationships continue to return to more normalized levels. Additionally, earnings growth is expected to improve substantially from last year and outpace that of large cap, which we believe provides further upside for the asset class. We believe active managers with a focus on quality should benefit as earnings growth becomes a more dominant driver of equity returns going forward.

Our current positioning is a function of our bottom-up security selection process and our ability to identify what we view as attractive investment candidates, regardless of economic sector definitions. Overweights in Information Technology and Industrials are broad-based with recent purchases across a variety of industries and end markets. Conversely, we continue to be underweight in Consumer Discretionary, as we have been unable to identify what we consider to be compelling opportunities that fit our discipline given the rising risk profiles as a result of structural headwinds for various brick and mortar businesses. While the portfolio's allocation to Health Care is roughly in line with the benchmark, we continue to be underweight in the biotechnology industry as many companies within that group do not fit our discipline due to their elevated levels of binary risk. Given our focus on long-term business fundamentals, patient investment approach and low portfolio turnover, the strategy's sector positioning generally does not change significantly from quarter to quarter; however, we may take advantage of periods of volatility by adding selectively to certain companies when appropriate. As always, our focus remains on identifying what we view as attractive, long-term investment opportunities that can create value for shareholders over the next three to five years, which we believe gives us the best opportunity to generate alpha for our clients.

Aristotle Small/Mid Cap Equity Composite Performance

All Periods Ended March 31, 2021



Year	Small/Mid Cap Equity Composite (Gross, %)	Small/Mid Cap Equity Composite (Net, %)	Russell 2500 Index (%)	Russell 2500 Value Index (%)
2021 YTD	9.76	9.65	10.93	16.83
2020	10.23	9.71	19.99	4.88
2019	23.73	23.25	27.77	23.56
2018	-10.22	-10.55	-10.00	-12.36
2017	13.98	13.24	16.81	10.36
2016	22.73	21.89	17.59	25.20
2015	3.77	3.17	-2.90	-5.49
2014	2.91	1.78	7.06	7.11
2013	38.34	37.41	36.82	33.32
2012	16.49	15.27	17.88	19.21
2011	0.00	-1.11	-2.51	-3.36
2010	28.17	28.07	26.70	24.82
2009	28.88	28.88	34.38	27.68
2008	-30.53	-30.53	-36.78	-31.99

Sources: SS&C Advent, Russell Investments

Composite returns for periods ended March 31, 2021 are preliminary pending final account reconciliation.

[1]The Aristotle Small/Mid Cap Equity Composite has an inception date of January 1, 2008 at a predecessor firm. During this time, Jack McPherson and Dave Adams had primary responsibility for managing the strategy. Performance starting January 1, 2015 was achieved at Aristotle Boston.

Past performance is not indicative of future results. Performance results for periods greater than one year have been annualized.

Returns are presented gross and net of investment advisory fees and include the reinvestment of all income. Gross returns will be reduced by fees and other expenses that may be incurred in the management of the account. Please see important disclosures enclosed within this document.