FUNDAMENTAL EQUITY

SMALL CAP

GREAT LAKES ADVISORS

A WINTRUST WEALTH MANAGEMENT COMPANY

MANAGER COMMENTARY

Second Quarter 2020

Ben Kim, CFA©, CPA
Head of Research
Senior Portfolio Manager

Senior Research Analysts
Ray Wicklander, III, CFA©
Huong Le, CFA©
Scott Schneider, CFA©
Scott Macke, CFA©
James Veers, CFA©

MARKET REVIEW

U.S. equities recovered sharply across the board during the second quarter, following the bloodbath of Q1. Year-to-date losses for larger-cap stocks now stand in the low single digits, while smaller-cap stocks have losses in the low double-digits.

The Russell 2000 index advanced 25.4% for the quarter, one of its three best quarters since the inception of the index. The rally was sparked by continued support from the U.S. Federal Reserve including the announcement that they would begin buying a broad and diversified portfolio of corporate bonds to support market liquidity. This was then followed by incrementally positive economic news throughout the quarter.

Stocks that were beaten down the most in March (micro-caps, lower-quality, and higher-levered companies) were the best performers in the quarter. This was not surprising, as they reacted in a manner consistent with past rebounds in recessionary periods. What was a bit unexpected was the continuation of growth stocks' outperformance versus value stocks. Value has now lagged during both the recovery and the market downturn. Growth outperformed value by 11.5% in the 2nd quarter (R2000 Growth +30.5% vs. R2000 Value +19.0%), and the R2000 Growth Index is 20.4% ahead of the R2000 Value Index (R2000 Growth -3.1% vs. R2000 Value -23.5%) for the first half of the year. The popular cohort of expensive, profitless stocks - biotechnology and software - continues to dominate the market in small cap. These two industries were the largest contributors to the index returns for the quarter as well as for the year to date. Biotechnology is up 12.5% and software is up 6.0%, while the Russell 2000 index is down nearly 13% for the six-month period ending June 30.

While our performance has been challenging, we are more excited for the long-term prospects of our portfolio than we have been in quite some time. Today, the quality of our portfolio stands out, and we believe it holds less risk than the index as we do not hold unprofitable, high-valuation stocks. The portfolio is extraordinarily cheap, trading at $0.50 cents on the dollar of value. In our opinion, our small cap portfolio is spring-coiled for attractive absolute and relative performance over the next several years.

SECOND QUARTER ATTRIBUTION

SECTOR	GLA WEIGHTING	GLA RETURN	R2000 WEIGHTING	R2000 RETURN	SECTOR ALLOCATION	STOCK SELECTION	ACTIVE CONTRIBUTION
Industrials	20.87	21.49	15.12	25.92	-0.00	-0.66	-0.66
Financials	20.43	22.63	18.51	12.20	-0.13	1.81	1.68
Consumer Disc.	17.00	20.31	11.14	51.37	1.41	-4.34	-2.93
Technology	12.41	20.69	15.38	28.36	-0.13	-0.78	-0.91
Health Care	8.73	31.84	21.61	31.79	-0.76	-0.09	-0.85
Materials	4.64	12.66	3.65	28.82	0.03	-0.85	-0.81
Comm. Services	4.23	9.32	1.25	12.33	-0.37	0.17	-0.20
Real Estate	3.06	2.46	4.51	14.03	0.20	-0.35	-0.15
Energy	2.35	-2.33	1.53	44.37	0.15	-1.03	-0.88
Consumer Staples	1.51	21.33	3.25	20.56	0.04	--	0.04
Utilities	--	--	3.93	-3.56	1.10	--	1.10
Cash	4.76	0.03	--	--	-1.32	--	-1.32
Total	**100**	**19.47**	**100**	**25.42**	**0.17**	**-6.12**	**-5.95**

Source: GLA, FactSet. Percentages may not add to 100% due to rounding. Peformance numbers are gross of fees.

The GLA Small Cap Strategy increased 19.5% during the quarter, compared to a 25.4% advance in the Russell 2000 index, underperforming the benchmark by 595 basis points.

On an absolute basis, all sectors except for energy contributed to returns, led by the industrial, financial, and consumer discretionary sectors.

The portfolio's underperformance relative to the index was due to unfavorable stock selection in the consumer discretionary, energy, and technology sectors. Additionally, our underweight position in healthcare and our mid-single digit cash position dragged on our relative performance. On the positive side of the ledger, financials was our biggest contributor to relative performance.

Stock Selection cost us 612 basis points of alpha while Sector Allocation contributed 17 bps of return:

- Stock selection within Consumer Discretionary was our largest detractor of relative performance, detracting 434 bps. All of our holdings were up, but they simply lagged the sharp recovery as some of our holdings held up better in the downturn.
- Stock selection in the Energy sector detracted 103 bps. Energy was the worst performing sector last quarter and bounced back strongly (+44%) this quarter with crude oil trading up 90% from its lows.
- Stock selection within the Technology sector detracted 78 bps. The technology sector outpaced the market, helped by continued strong returns from expensive, unprofitable growth stocks as investors continue to buy stocks that have worked and sell stocks that have not. We have generally avoided these businesses as we believe that the current valuations the market is conveying on these companies do not allow for downside protection should fundamentals fail to play out.
- Strong stock selection in Financials added 181 basis points of relative contribution.
- In aggregate, our Healthcare performance was in line with the sector's performance. However, our underweight exposure cost us 76 basis points of alpha. We are satisfied with this given biotechnology's strong outperformance in the sector, which was up 40%. Our portfolio does not have an allocation to biotechnology as these companies do not have earnings.

MARKET OUTLOOK

This quarter reveals the exceptional nature of this COVID-19-driven recession (as formally declared by the NBER). And this says little or nothing of the massive dislocation of the oil market, the unprecedented fiscal and monetary policy responses, and the social and political unrest in the country at this time. And the financial markets appear to be confounding many an investment legend, from Cliff Asness to David Tepper to Stan Druckenmiller and even Warren Buffet.

But we must ground ourselves in data. As Sherlock Holmes said: "Data! Data! Data! ... I can't make bricks without clay."

A number of widely-followed economic indicators hit record levels, some by a wide margin. Among the data which highlight the damage:

- Highest level of unemployment since the Great Depression
- Consumer Confidence falls off a cliff
- Retail sales drop the most on record during April
- Industrial Production posts its sharpest monthly decline
- Capacity Utilization hits record low
- Leading Economic Indicators turn negative; Coincident to Lagging Indicators hitting all-time low
- Housing permits, starts, and existing home sales plunged early in Q2
- Oil Prices drop below $0 briefly, and Goldman Sachs Commodity Index hits 30+ year low

The collective policy response to the first wave of COVID-19 has been quite effective. Financial conditions have eased substantially as the Fed's balance sheet swelled by some 85% over the past 10 months (recall, quantitative easing actually began last September) and M2 leapt by 20%+. This led to a string of positive economic surprises as the quarter wore on. Yields on 10yr Treasuries remain near record lows, the USD remains strong – even while Gold approaches a record high – quality spreads have narrowed, and home prices have remained surprisingly resilient. A true second wave could, however, bring about the need for additional stimulus.

The U.S. equity market appears to have priced in a pretty solid and quick recovery scenario. By almost any traditional valuation metric (granted, valuation metrics under this type of economic volatility are iffy), U.S. equities are expensive. The exception points to TINA* as the excuse to drive sustained gains: both the S&P 500 and Russell 2500 are inexpensive relative to bonds as measured by the Equity Risk Premium.

*TINA: There is no alternative

Financial Advisors please contact us at
sma@greatlakesadvisors.com

Institutional Investors please contact us at
cr@greatlakesadvisors.com

Chart Source: FactSet

The data in the attribution table represent the returns for each sector and the gross returns for a representative composite account for one quarter ending the current calendar quarter. Individual account returns may vary.

Great Lakes Advisors, LLC ("Great Lakes" or "GLA") is an investment advisor registered with the Securities and Exchange Commission under the Investment Advisors Act of 1940. Established in 1981, Great Lakes is a subsidiary of Wintrust Financial Corporation and a part of the Wintrust Wealth Management family of companies. On October 1, 2013, majority owned subsidiary Advanced Investment Partners, LLC ("AIP") became fully-owned and integrated into Great Lakes. Great Lakes is a distinct business unit with distinct investment processes and procedures relating to the management and/or trading of investment portfolios for its clients.

Great Lakes Advisors, LLC claims compliance with the Global Investment Performance Standards (GIPS®). A complete list of firm composites and performance results, and the policies for valuing portfolios, calculating performance, and preparing GIPS compliant presentations are available upon request. Great Lakes Advisors, LLC's fees are available upon request and may be found in our Form ADV Part 2A. Performance data quoted herein represents past performance. Past performance does not guarantee or indicate future results. Returns and net asset value will fluctuate.

Manager commentary represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice. To determine if this strategy is appropriate for you, carefully consider the investment objectives, risk factors, and expenses before investing. The holdings, industry sectors, and asset allocation are presented to illustrate examples of the securities bought and the diversity of areas in which we may invest, and may not be representative of current or future investments. Portfolio holdings subject to change and should not be considered investment advice. The specific securities identified and described do not represent all of the securities purchased, sold or recommended for advisory clients and it should not be assumed that investments in the securities identified and discussed were or will be profitable. To obtain a list of all securities recommended during the past year, contact Great Lakes Advisors (GLA) at 312.553.3700. Actual clients' portfolios may or may not hold the same securities depending on the guidelines, restrictions and other factors of the specific portfolios.

Frank Russell Company ("FRC") is the source and owner of the Russell Index data contained or reflected in this material and all trademarks and copyrights related thereto. The presentation may contain confidential information and unauthorized use, disclosure, copying, dissemination, or redistribution is strictly prohibited. This is a GLA presentation of the Russell Index data. Frank Russell Company is not responsible for the formatting or configuration of this material or for any inaccuracy in GLA's presentation thereof.

Standard and Poor's, a division of the McGraw-Hill Companies, Inc., is the owner of the trademarks and copyrights relating to the S&P Index. The product is not sponsored, endorsed, sold or promoted by Standard and Poor's. Standard and Poor's makes no representation regarding the advisability of investing in the Product.

The index performance figures are calculated in U.S. dollars and reported on a gross basis. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Fees, including but not limited to the advisory fee, transaction and custody charges, would reduce the return. Investors cannot invest directly in an index. These indexes are not managed or sold by Great Lakes Advisors. Past performance is not indicative of future results. 20-6-0122