

**OBJECTIVE**

Invests in municipal bond Exchange Traded Funds (ETFs), diversified across maturities and a wide variety of municipalities. These ETFs produce income generally exempt from federal income taxes. Strives to deliver the income and lower volatility traditionally available from a diversified municipal bond portfolio.

**INVESTMENT PHILOSOPHY & PROCESS**

Fixed Income Tax-Exempt invests in municipal bond ETFs with domestically oriented, investment-grade benchmarks. These ETFs produce income that is generally exempt from federal income taxes. The investment approach incorporates ETFs with a national, not state-specific, posture. It is constructed to have characteristics similar to a traditional, laddered bond portfolio and its benchmark is the ICE BofA U.S. Municipal Securities Index. The Confluence Fixed Income Strategy Committee may adjust the portfolio duration and maturity to be longer, shorter or in line with this benchmark. The investment committee incorporates its viewpoints regarding Fed policy, the shape of the yield curve, relative yields, credit spreads, default rates and other market factors into the portfolio construction process.

The strategy invests in a range of maturity-date ETFs to construct a portfolio similar to a diversified bond ladder, and complements these positions with traditional fixed income ETFs with more "static" maturity profiles, allowing for more precise exposures to maturities and sectors of the bond market. The Fixed Income Strategy Committee continuously monitors the portfolio, rebalancing at least annually, but may elect to rebalance over shorter time frames at its discretion. The investment committee may direct larger allocations to certain ETFs to alter the nature of maturity exposures in a portfolio.

Fixed Income Tax-Exempt is available as a standalone portfolio and may also be available as part of a Balanced account, which allows investors to combine this fixed income strategy with one of the firm's equity strategies in one portfolio.

(Allocations as of 7/19/2022 rebalance)

**OVERVIEW**

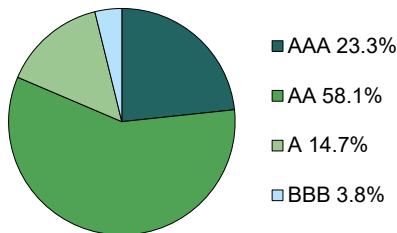
- ◆ Strives to deliver income and lower volatility traditionally available from a diversified municipal bond portfolio
- ◆ Uses high-quality ETFs following investment grade benchmarks with domestic orientation that provide income exempt from federal income tax
- ◆ Similar characteristics to traditional bond ladder or diversified bond index by combining use of maturity-date ETFs with traditional fixed income ETFs
- ◆ Allocations incorporate viewpoints on Fed policy, yield curve shape, relative yields, credit spreads, default rates, etc.
- ◆ Nationally diversified across maturities and municipalities; not managed on a state-specific basis
- ◆ Available as a standalone portfolio or in Balanced accounts combined with equity strategy

**CHARACTERISTICS<sup>1</sup>**

(WEIGHTED AVERAGE)

|  |       |
|--|-------|
| SEC Yield  | 2.8%  |
| Tax-Equivalent SEC Distribution Yield Estimate*        | 4.2%  |
| <small>*Assumes Federal Income Tax Rate of 35%</small> |       |
| Duration   | 6.9   |
| Maturity   | 10.4  |
| ETF Expense Ratio                                      | 0.18% |

**RATING CATEGORIES<sup>1</sup>**

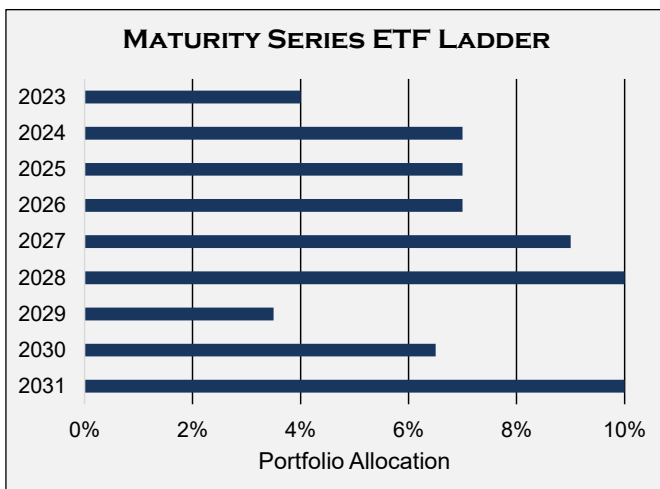


**SECTOR ALLOCATION<sup>1</sup>**

|                    |       |
|--------------------|-------|
| General Obligation | 30.8% |
| Advance Refunded   | 2.0%  |
| Revenue            | 67.2% |

<sup>1</sup>This information is presented as supplemental information to the disclosures required by the GIPS® standards. Sector allocations shown represent the model portfolio as of 7/19/22 and do not represent the precise allocation in an actual client account. Allocations in client accounts may vary based on individual client considerations and market fluctuations. The allocation of assets in the model portfolio may change from time to time due to market conditions and economic factors. Investments are not guaranteed and do carry a risk of loss of principal. Each asset class has specific risks associated with it and no specific asset class can prevent a loss of capital in market downturns. The listing of "5 Largest Holdings" is not a complete list of all ETFs in the portfolio or which Confluence may be currently recommending. Application of the investment strategy as of a later date will likely result in changes to the listing. Individual client portfolios may differ, sometimes significantly, from these listings. Contact Confluence for a complete list of holdings. Yield data source: Morningstar; 30-day SEC yield of the model portfolio as of 7/19/22. Duration and maturity figures shown are based on all holdings in the model portfolio as of the rebalance date. ETF expense ratio is in addition to Confluence management fees. Rating categories reflect S&P ratings; source: Morningstar.

**MATURITY SERIES ETF PROFILE<sup>2</sup>**



Fixed Income Tax-Exempt utilizes a portfolio structure similar to that of a "bond ladder," a tactic often used when purchasing individual bonds. With our approach, we instead create a ladder of maturity-series ETFs. These ETFs hold large pools of bonds that mature near to, but always before, a specified end date. Accordingly, with the passage of time, the average maturity of this kind of ETF naturally shortens, thereby replicating some characteristics of an individual bond. It's not exactly the same, particularly because it doesn't mature at a par value. However, the maturity-series ETF has more credit risk diversification, while oftentimes also providing liquidity improvement, relative to an individual bond.

The strategy has ladder "rungs" from end dates ranging between 2023 and 2031. We believe this laddered approach positions investors to participate in a wider range of yields, while also providing a mechanism to help address the risk of rising interest rates. If rates were to rise, the shortest "rung" could be sold, or allowed to reach its end date. The proceeds could then be redeployed into a longer "rung," one with a higher yield.

<sup>2</sup> Holdings in client accounts may vary based on individual client considerations and market fluctuations. The model portfolio may change from time to time due to market conditions and economic factors. Investments are not guaranteed and do carry a risk of loss of principal. Although fixed income ETFs, including maturity-series ETFs, invest in bonds, they have many differences relative to an individual bond and may trade significantly above or below the stated net asset value. ETFs trade like a stock but charge internal management fees; there will be brokerage commissions associated with buying and selling ETFs. This information is presented as supplemental information to the disclosures required by the GIPS® standards.

## JULY 2022 FIXED INCOME TAX-EXEMPT MARKET OBSERVATIONS

- ◆ Treasury yields continued to rise in the second quarter, creating a headwind for the municipal bond market.
- ◆ The flat yield curve indicates a growing likelihood of recession, which could foster lower inflation and even a reversal toward easier policy by the Fed.
- ◆ The portfolio duration remains in line with the benchmark, with a heavier weight to revenue bonds and an underweight to general obligation bonds (GOs).

During the second quarter of 2022, the Confluence Fixed Income Tax-Exempt return of -3.5% (gross of fees) was shy of the benchmark return of -3.3%. Year-to-date, our strategy gross return was -10.1% versus -9.3% for the benchmark. [Strategy net-of-fees returns for the same periods were -4.2% QTD and -11.4% YTD. See disclosures below for fee description; actual investment advisory fees may vary.]

In response to tighter Fed policy, Treasury yields rose in the second quarter and created a headwind across all sectors of the municipal bond market. Yields rose the most for maturities of less than one year as the market responded to higher short-term rates directed by the Fed. Longer-maturity yields rose comparatively less, but the price impact was much higher. Accordingly, the most negative returns in the municipal bond market during the quarter came from the longest maturities.

Looking forward, attention remains focused on the Fed, inflation, and how tighter monetary policy will affect the economy. The bond market has already priced in several increases in the Fed's short-term rate as indicated by Treasury yields approaching 3% for six-month maturities. It's noteworthy that Treasury yields remain below 3.5% for longer maturities, even those extending out to 30 years. This flat yield curve profile reflects a growing possibility that a recession may result from tighter Fed policy, and it could be accompanied by lower inflation and even a reversal by the Fed toward easier monetary policy.

For these reasons, we believe a posture diversified across maturities is appropriate, including the use of laddered maturities. This position allows investors to participate in higher intermediate yields, while also having some exposure to shorter maturities, which could be reinvested into higher yields if rates continue to rise. At the same time, a smaller exposure to longer maturities helps address risks associated with recession and geopolitical factors. Accordingly, the strategy includes a wide range of exposures, but is centered on intermediate maturities. The overall duration is 6.9 years, which is very close to the benchmark duration of 6.8 years. Although there have been strong tax collections and elevated reserves by state and local governments, we remain underweight GOs. We think there is a greater advantage in revenue bonds, especially transportation and essential services such as water and sewer districts.

Information provided in this report is for educational and illustrative purposes only and should not be construed as individualized investment advice or a recommendation. The investment or strategy discussed may not be suitable for all investors. Investors must make their own decisions based on their specific investment objectives and financial circumstances. Opinions expressed are current as of the date shown and are subject to change.

### PERFORMANCE COMPOSITE RETURNS (FOR PERIODS ENDING JUNE 30, 2022)

|                   | Pure Gross-of-Fees <sup>1</sup> | Net-of-Fees <sup>2</sup> | Benchmark (BofA/Muni) | Calendar Year | Pure Gross-of-Fees <sup>1</sup> | Net-of-Fees <sup>2</sup> | Benchmark (BofA/Muni) | Difference (Gross-Benchmark) | # of Portfolios | Composite Assets (000s) | Total Firm Assets (000s) | Composite 3yr Std Dev | Benchmark 3yr Std Dev | Composite Dispersion |
|-------------------|---------------------------------|--------------------------|-----------------------|---------------|---------------------------------|--------------------------|-----------------------|------------------------------|-----------------|-------------------------|--------------------------|-----------------------|-----------------------|----------------------|
| Since Inception** | 1.2%                            | (1.8%)                   | 3.0%                  | 2010**        | (3.4%)                          | (4.1%)                   | (4.5%)                | 1.1%                         | 1               | \$48                    | \$751,909                | N/A                   | N/A                   | N/A                  |
| 10-Year*          | 1.0%                            | (2.0%)                   | 2.5%                  | 2011          | 6.5%                            | 3.3%                     | 11.2%                 | (4.7%)                       | 1               | \$51                    | \$937,487                | N/A                   | N/A                   | N/A                  |
| 5-Year*           | 0.5%                            | (2.4%)                   | 1.5%                  | 2012          | 2.0%                            | (1.0%)                   | 7.3%                  | (5.3%)                       | 1               | \$52                    | \$1,272,265              | N/A                   | N/A                   | N/A                  |
| 3-Year*           | (1.0%)                          | (3.9%)                   | (0.2%)                | 2013          | (1.1%)                          | (4.1%)                   | (2.9%)                | 1.7%                         | 1               | \$52                    | \$1,955,915              | 2.4%                  | 4.4%                  | N/A                  |
| 1-Year            | (10.0%)                         | (12.7%)                  | (8.9%)                | 2014          | 4.0%                            | 0.9%                     | 9.8%                  | (5.8%)                       | 3               | \$600                   | \$2,589,024              | 2.2%                  | 4.1%                  | N/A                  |
| YTD               | (10.1%)                         | (11.4%)                  | (9.3%)                | 2015          | 1.9%                            | (1.2%)                   | 3.6%                  | (1.7%)                       | 4               | \$2,678                 | \$3,175,419              | 2.1%                  | 3.7%                  | 0.0%                 |
| QTD               | (3.5%)                          | (4.2%)                   | (3.3%)                | 2016          | (0.8%)                          | (3.8%)                   | 0.4%                  | (1.3%)                       | 5               | \$2,983                 | \$4,413,659              | 3.3%                  | 3.4%                  | 0.1%                 |
|                   |                                 |                          |                       | 2017          | 4.1%                            | 1.0%                     | 5.4%                  | (1.3%)                       | 5               | \$3,073                 | \$5,944,479              | 3.4%                  | 3.2%                  | 0.0%                 |
|                   |                                 |                          |                       | 2018          | 0.8%                            | (2.2%)                   | 1.0%                  | (0.2%)                       | 4               | \$2,961                 | \$5,486,737              | 3.5%                  | 3.3%                  | 0.0%                 |
|                   |                                 |                          |                       | 2019          | 5.5%                            | 2.4%                     | 7.7%                  | (2.2%)                       | 3               | \$2,931                 | \$7,044,708              | 2.2%                  | 2.4%                  | 0.0%                 |
|                   |                                 |                          |                       | 2020          | 5.4%                            | 2.3%                     | 5.3%                  | 0.2%                         | 3               | \$3,210                 | \$6,889,798              | 3.9%                  | 4.1%                  | 0.0%                 |
|                   |                                 |                          |                       | 2021          | 0.8%                            | (2.2%)                   | 1.8%                  | (1.0%)                       | 3               | \$3,274                 | \$7,761,687              | 4.0%                  | 4.0%                  | 0.0%                 |

\*Average annualized returns

\*\*Inception is 10/1/2010

#### Portfolio Benchmark

ICE BofA U.S. Municipal Securities Index (Source: Bloomberg)

Confluence Investment Management LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Confluence Investment Management LLC has been independently verified for the periods August 1, 2008, through December 31, 2021. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards.

Verification provides assurance on whether the firm's policies and procedures related to composite maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report.

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The Fixed Income Tax-Exempt strategy was inceptioned on October 1, 2010, and the current Fixed Income Tax-Exempt Composite was created on May 1, 2014. Confluence Investment Management LLC is an independent registered investment adviser. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

<sup>1</sup> Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

<sup>2</sup> Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite is as follows: 0.40% on the first \$500,000; 0.35% on the next \$500,000; and 0.30% over \$1,000,000. There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Subsequent to May 1, 2014, bundled fee accounts make up 100% of the composite for all periods. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Performance prior to May 1, 2014, is based on the Fixed Income Tax-Exempt-Direct Composite which was created on October 1, 2010. The Fixed Income Tax-Exempt-Direct Composite includes accounts that pursue the Fixed Income Tax-Exempt strategy, but do not have bundled fees. Gross returns from the Fixed Income Tax-Exempt-Direct Composite include transaction costs and net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. A complete list of composite descriptions is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. The annual composite dispersion is an equal-weighted standard deviation, using gross-of-fee returns, calculated for the accounts in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Fixed Income Tax-Exempt Composite contains fully discretionary Fixed Income Tax-Exempt wrap accounts. The Fixed Income Tax-Exempt portfolio utilizes bond ETFs to earn tax-exempt income.

\*\*Results shown for the year 2010 represent partial period performance from October 1, 2010, through December 31, 2010. N/A-Composite Dispersion: Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. N/A-3yr Std Dev: Composite does not have 3 years of monthly performance history.

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#### The Confluence Mission

Our mission is to provide our clients with superior investment solutions and exceptional client service with the highest standards of ethics and integrity. Our team of investment professionals is committed to delivering innovative products and sound, practical advice to enable investors to achieve their investment objectives.

#### ABOUT CONFLUENCE INVESTMENT MANAGEMENT LLC

Confluence Investment Management is an independent Registered Investment Advisor located in St. Louis, Missouri, that provides professional portfolio management and advisory services to institutional and individual clients. Confluence's investment philosophy is based upon independent, fundamental research that integrates evaluation of market cycles, macroeconomics and geopolitical analysis with the firm's value-driven approach. The investment team's portfolio management philosophy begins by addressing risk and follows through by positioning clients to achieve income and growth objectives.

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