U.S. Large Cap Growth Commentary

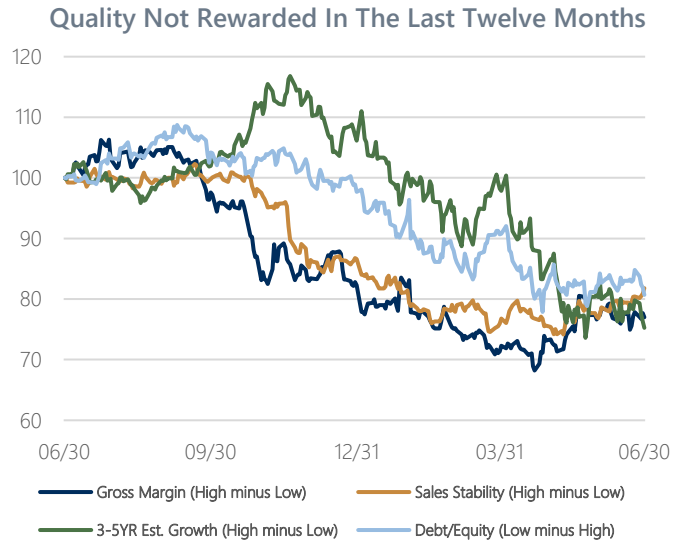
Q2 2022

SGA Sustainable Growth Advisers

Performance

The U.S. Large Cap Growth portfolio returned -20.1% (gross) and -20.2% (net) in Q2 versus -20.9% for the Russell 1000 Growth Index. Market returns were weak due to growing concerns that higher interest rates would threaten future economic and corporate profit growth. Broad market returns for the first half of the year were the worst since 1970.

Within the Russell 1000 Growth Index, better business quality metrics were rewarded later in the quarter after having underperformed for much of the past year.



Source: FactSet, Russell

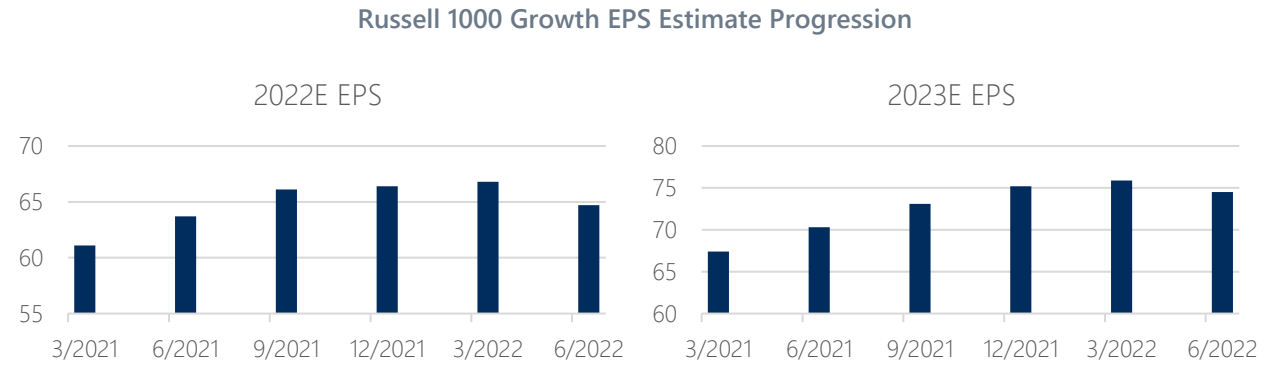
Highlights

- Portfolio marginally outperformed the Russell 1000 Growth Index in Q2; business quality characteristics began to be rewarded later in the quarter after having underperformed over the last year
- Companies with the highest forecasted growth underperformed by the widest margin posing a headwind for our approach
- Positions in IQVIA and UnitedHealth contributed most to portfolio performance, while positions in Amazon, Workday, and Illumina detracted most
- RingCentral, PayPal, and Illumina were sold due to competitive concerns as more attractive higher confidence growth opportunities emerged given increased market volatility; positions in Adobe and IQVIA were established
- Portfolio is more attractively valued than the market with better business quality and forecast growth; well positioned for an environment of continued high volatility and slowing economic growth

Consensus Earnings Expectations for the Market Remain Too High

The U.S. government reported the highest Consumer Price Index (CPI) reading recorded since 1981 at +8.6%. Gasoline prices hit a record high of over $5 dollars per gallon while food and housing prices continued to increase contributing to the University of Michigan's Consumer Sentiment Index reporting its lowest reading on record going back to 1952.

In response to higher inflation levels, the Fed raised interest rates by 50 bps in May and another 75 bps in June following its 25 bps increase in Q1 with further increases expected in July. While the economy continues to show positive momentum for now, weakening consumer sentiment, cracks in the labor market exposed by recent layoff announcements, and expected declines in industrial production drive our continued belief that consensus earnings growth expectations for the market are too high. Accordingly, we expect to see significant reductions in earnings forecasts from today's levels over the course of the second half of 2022 and into 2023.



Source: FactSet, Russell

Key Contributors and Smallest Detractors

A position in **IQVIA** was initiated during the quarter and was the largest contributor to portfolio performance given its short time in the portfolio in a declining market. We are excited by IQVIA's growth prospects and look forward to building the position opportunistically moving forward. A thorough writeup of our thesis is included in the Purchases section below.

UnitedHealth was the second largest contributor to portfolio performance. The company benefited from the market's preference for Health Care stocks in Q2. The company also reported Q1 results that were in line with our expectations with strong results from Optum. OptumHealth's revenue per consumer grew by 33%, driven by an increasing number of patients served under value-based care arrangements. OptumRx performed well in the quarter and is expected to benefit further next year given the expected launch of multiple new biosimilars in the U.S. Enrollments in the UnitedHealthcare benefits business were slightly below our expectations for the quarter, but we see no negative trend there. Also, the company's large floating rate investment portfolio likely benefited the stock because its earnings increase by almost 1% for each 1% increase in interest rates. We maintained an above-average weight in the company during the quarter, trimming on recent strength.

Yum! Brands was the smallest detractor from performance in Q2 after it posted in line Q1 results with strong unit growth exceeding management's long-term guidance and robust Taco Bell comps offsetting both COVID-driven weakness in China and a drag from the company's decision to suspend operations in Russia. The company maintained its full year 2022 top line guidance but reduced its forecast earnings growth from high-single-digit to mid-single-digit growth to reflect the discontinuation of contributions from Russia. With about 50% of the company's stores in China closed in Q1 due to lockdowns, there should be room for meaningful improvement over the course of the second half of the year. We continue to view Yum! Brands as a very resilient business with an improving growth algorithm trading at a reasonable valuation. We maintained an average weight position in the company during the quarter, trimming on recent strength.

The second and third smallest detractors from portfolio performance were **RingCentral** and **Adobe.**

Key Detractors

Amazon was the largest detractor from portfolio performance in Q2 driven by its large average weight of 5.8% in the portfolio and its relative underperformance. The stock declined significantly during the quarter after holding up relatively well in the first quarter of the year as more short-term focused investors were disappointed after the company's guidance for Q2 fell short of expectations. The company's Q1 results showed Amazon Web Services (AWS) posting 37% year-over-year sales growth which was in line with expectations, advertising growing 24% year-over-year in line with our expectations, and Amazon Retail, in line with their domestic business outperforming international. However, the company noted headwinds from rising costs, excess hiring that has not yet been absorbed and become productive, and costs from new fulfillment capacity added which likewise is not yet fully utilized or productive. The company has begun instituting price increases to address the inflation impact, while the excess hiring impact should fade in Q3 and Q4 as the new associates are fully onboarded and integrated. We expect that the extra fulfillment capacity they have created will take longer to turn productive, but in the meantime, this should lead to a reduction in capex expenses. We also note the movement of Prime Day from Q2 to Q3 and the impact that will have on Q2 results.

We have adjusted our forecasts to take into account the issues noted above but see those as temporary impediments which will be addressed within our time horizon. We remain positive on Amazon's growth opportunities looking forward, particularly in AWS and the company's advertising opportunity, and acknowledge the more difficult operating environment for the retail segment. With strong operating performance overall and a reduced valuation given the market's preference for other areas over the last year, we remain confident in the position and added to it on weakness during the quarter.

Workday was the second largest detractor from performance in Q2. The company was penalized along with other software-oriented companies during the quarter given the market's preference for slower growth businesses. Also affecting performance was concern by some investors after the company's Q1 backlog showed growth of 21%, just shy of management's 22% guidance. This led some to speculate over the impact on its business from slowing economic activity. Management asserted that the reason for the shortfall was a couple of larger deal closings slipping from one quarter to the next. Q2 guidance for backlog was maintained at 20% growth, consistent with Workday's 3-year targeted 20% revenue growth, and customer retention remained strong at 95%. Revenue guidance for the year was raised slightly. Otherwise, results were in line with our expectations, and we remain positive on Workday's opportunity to capitalize on the secular shift in human resources enterprise software from on-premises to software-as-a-service solutions as well as increased international penetration and cross-selling of its broadening portfolio of services into its already expanding installed base. We remain confident in the company's prospects and added to the position on weakness during the quarter.

Illumina was the third largest detractor from portfolio performance in Q2 despite the company reporting solid Q1 earnings per share. Revenues increased 12% year-over-year with its Instruments segment growing 20% and Sequencing Consumables growing 13%. The company saw continued improvement in insurance coverage for sequencing and exited the quarter with record high Consumable and Instrument backlogs. Margins continued to be good but ramping up investments in GRAIL can be expected to impact earnings. Management guidance for Q2 was cautious leading to some concerns about their fiscal year guidance. Weakness in the Biotech sector and concern over Biotech research funding generally posed a headwind for the stock despite its overall solid results for the quarter. By region, Illumina's results in the Americas and Japan drove the company's growth with 15% and 33% growth on a year-over-year basis, respectively. Results in EMEA and China were weak due to sales in Russia and the impact of China's COVID lockdowns. Given declining confidence, the position was liquidated during the quarter. The rationale is noted in the Sales section below.

The fourth and fifth largest detractors from performance in Q2 were **Netflix** and **Match.**

Portfolio Activity

Turnover in the portfolio increased marginally during the quarter in response to higher levels of volatility in the market and new valuation opportunities in Qualified Company List businesses. During the quarter, we liquidated positions in RingCentral, PayPal, and Illumina due to competitive concerns given increased uncertainty in each and more attractive valuations in more predictable businesses. We initiated positions in Adobe and IQVIA. During the quarter we also trimmed positions in Visa, Autodesk, FleetCor, UnitedHealth, Yum! Brands, Thermo Fisher, Abbott, and Workday earlier in the quarter, on strength. We purchased additional shares of Ecolab, Amazon, Microsoft, Regeneron, and Workday among others on weakness.

Purchases

Taking advantage of weakness in high quality software-as-a-service companies' share prices, we initiated a position in creative design and document cloud management company **Adobe** in Q2. Its key focus is making specialized software tools for graphic designers. The company offers a Creative Cloud suite of design software tools as well as its Document Cloud management platform that includes the Acrobat PDF document maker and the Experience Cloud marketing technology platform. Adobe Creative Cloud is the dominant player in the graphic design software market, particularly for professional designers. Document Cloud allows users to view, create, and manage electronic documents and signatures while Experience Cloud provides users with a stack of marketing analytics, content management, advertising, and e-commerce tools.

Adobe benefits from strong pricing power given its dominant position in the Creative Cloud segment where no competitor has a comparable set of offerings. Creating a suite of products with similar breadth would be a huge and long-term task as designers build their careers around their Creative Cloud skills. For a similar reason, Adobe enjoys strong recurring revenue streams given its dominant position and the difficulty businesses would face in changing vendors due to their established

work processes incorporating Adobe tools. The company's growth is ultimately driven by an ever-expanding market of digital content demand, with an estimated 700 million "communicators" and over 4 billion consumers of the content. Importantly, Asia still only accounts for about 15% of the company's total sales. Additionally, document digitization remains in an early stage with a significant proportion of the company's license users not having yet moved to Adobe's software-as-a-service model. With the company generating attractive free cash flow, which we forecast to steadily increase over the coming years, Adobe provides the strong financial characteristics we seek.

Among the key risks we are monitoring with the company is regulation given that Adobe has over 90% market share in the graphic design software space. We are also cognizant that the company historically had a cyclical element to it, but its business model has shifted since then from a licensing model to a subscription-based software-as-a-service model which has led to recurring revenues increasing from 5% in 2007 to about 92% today. Finally, we will be monitoring Adobe's ecosystem for emerging competition.

In June, we initiated a below-average weight position in **IQVIA** which is a leading global provider of advanced analytics, technology solutions, and clinical research services to the Life Sciences industry. IQVIA was created in 2016 from the combination of IMS Health, a leading information and technology services company for the healthcare industry, and Quintiles, the largest provider of biopharma development services and commercial outsourcing services. The company has over 60 years of experience in sourcing, cleansing, and organizing healthcare data that is deeply integrated into the workflows of over 8,000+ clients. Integrating its data capabilities with its technology applications and consulting services, IQVIA offers a one-stop shop to clients, saving them valuable time and money as they work to bring new products to market. While about 49% of the company's revenues are derived from the Americas, IQVIA gets about 29% of its revenues from Europe and 20% from the Asia-Pacific region.

The company possesses attractive pricing power given a wide moat based on its experience in and ability to provide superior data and analytics integration to customers avoiding the need to hire third party IT consultants and expediting customer product launches. It generates high recurring revenues with about 25% of its total revenue tied to contracts or subscriptions that offer 90-95% renewal rates and an additional 50% of revenues derived from Research & Development which results from a backlog of business with up to 3-year revenue visibility. We expect to see high teens earnings growth from IQVIA over the coming three years on the back of high-single-digit revenue growth. The company's long-term growth opportunity is supported by the increased demand for contract research organizations (CRO's) by biopharmaceuticals who prefer to outsource their data and analytics needs to companies with broad capabilities and wide therapeutic expertise which can assist them in bringing new products to market more efficiently. We expect the company to gain market share due to its ability to offer a unique combination of data, analytics, technology, consulting, and clinical trial services as it continues to expand its scale.

The key risks associated with the position are the company's level of investment and its impact on margins, the continued rate of biotech funding which is strong relative to history, and the company's higher level of leverage due to the merger. Leverage ratios are declining, and we expect that to continue.

Sales

During the quarter we sold the portfolio's position in **PayPal**. We had maintained a below-average weight position in the stock following a change in the company's growth focus from attracting new users to enhancing platform utilization from existing users which raises concern over the company's growth runway. We were also disappointed by management's notice that some of the user growth which occurred during the pandemic appeared to be of lower quality with such customers utilizing PayPal less frequently in the post-pandemic environment. With concern over rising competition in an increasingly crowded field, disappointment over changes in management and weakening confidence in the company's execution, particularly with regard to the long-awaited development of the company's digital wallet, we sold the stock to take advantage of other more predictable growth opportunities created in the quarter's market volatility.

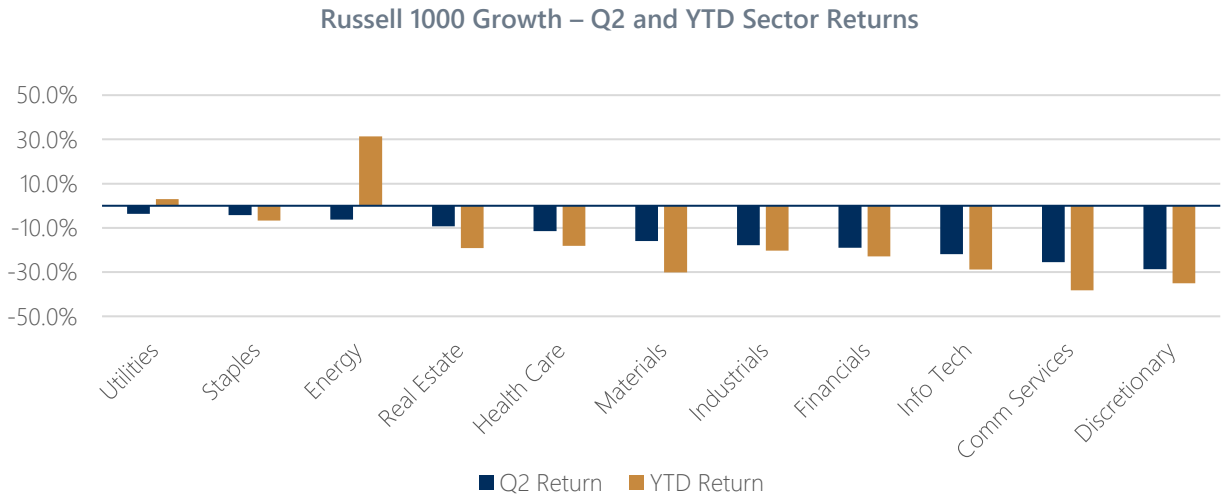
The portfolio's position in **Illumina** was liquidated during the quarter due to forced attrition. Given ongoing concerns about the dilution from the GRAIL acquisition, and uncertainty over the regulatory decision with regard to the acquisition, and the fact that Illumina faces potential competition in its core business, we had maintained a below-average weight position in the stock. The announcement during the quarter of the CFO's planned departure also elevated our concern regarding the

uncertainty of GRAIL's growth trajectory and earnings dilution moving forward. Given market weakness and the fact that a larger proportion of the company's earnings growth came in the later years of our analysis, we sold the position to fund the purchase of other higher confidence opportunities which offered better growth at a more attractive valuation.

The portfolio's position in **RingCentral** was liquidated as our confidence in our thesis for the company weakened due to a combination of upper management departures and increasing competition in the space. Given the small initial size of our position and our focus on either bringing it to a full size on weakness or moving on to other higher confidence opportunities that have developed, we chose the latter. We continue to see good opportunity in the software-as-a-service based communication market but expect RingCentral to face greater competition as it seeks to capitalize on the opportunity and have some reservations over the extent of the changes which have occurred in the management team.

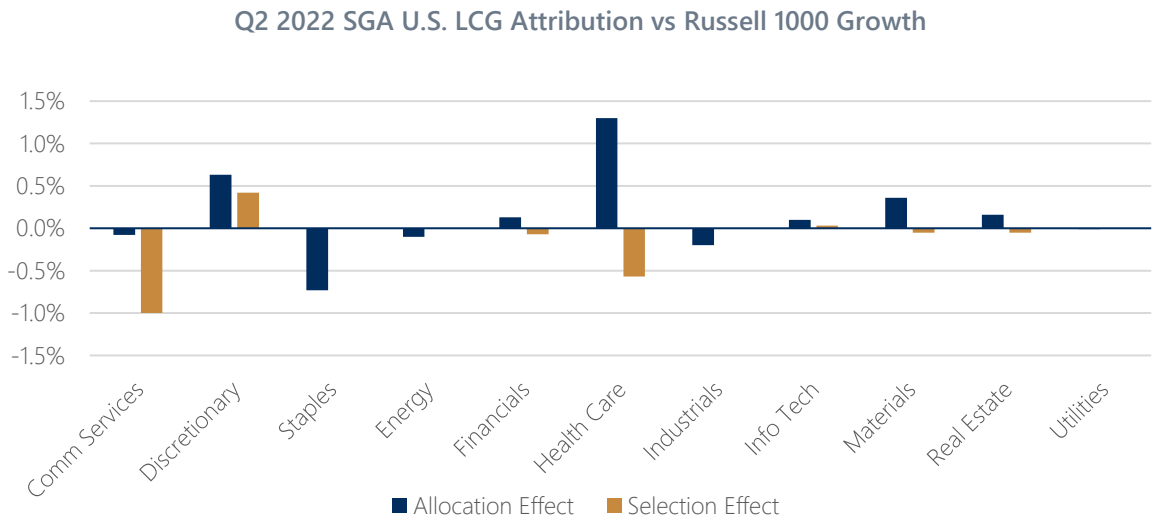
Portfolio Attribution

More defensive areas of the market and Energy outperformed reflecting rising oil prices and growing investor concern over the chances of a recession in the U.S. This shift in focus by investors away from inflation and rising interest rates and toward economic slowing and possible recession led to a shift in style preferences later in the quarter with growth factors showing some improvement.



Source: FactSet, Russell

The portfolio's overweight in Health Care and underweight in Consumer Discretionary stocks benefited relative returns while no exposure to the more defensive Consumer Staples, or Industrials and Energy sectors detracted. Stock selection in the Communication Services and Health Care sectors detracted from the portfolio's relative performance due primarily to positions in Netflix, Match Group, and Illumina. Positive selection in the Consumer Discretionary sector benefited relative returns due to the portfolio's position in Yum! Brands. The portfolio's exposure to companies with higher earnings growth rates hurt relative performance given rising interest rates and the market's evolving concern over slowing economic growth.



Source: FactSet, Russell

Outlook

Over the last year, forecast earnings estimates for 2022 and 2023 for the broader market have risen and company earnings reports have generally been solid despite the emergence of multiple headwinds to future growth. With rising interest rates, less fiscal stimulus, weakening consumer sentiment, signs of weakening employment, and the expectation for declining industrial production, we believe the Russell 1000 Growth Index and the broader market indexes will suffer reduced earnings growth expectations. The sustainable revenue growth and compounding cash flow of SGA portfolio companies provide a solid foundation in such an environment, while our focus on buying the growth streams at attractive valuations should make the portfolio less susceptible to further multiple contraction. To that end, we currently utilize an average discount rate of about 10% in our Discounted Cash Flow calculations.

Meanwhile, the superior pricing power we demand from our companies, and their commensurate ability to protect margins in a period of high inflation, also helps position the portfolio more effectively for the inflationary headwinds buffeting the market today. As higher interest rates and steeply higher energy prices kick in, economic growth should slow, removing the tailwind that has boosted economically sensitive companies off pandemic lows. While the past 18 months have been difficult for our portfolio's relative performance, the pro-cyclical environment that posed such a headwind looks to be fading. We remain confident in the growth our portfolio companies offer and expect their share prices to be rewarded as the economic tide turns. We expect the portfolio to generate 16% earnings growth and 12% revenue growth over the next three years versus 12% and 13%, respectively for the Russell 1000 Growth Index, which we, again, believe will be revised downward.

We thank you for your continued support and your confidence in our team.

The opinions expressed herein reflect the opinions of Sustainable Growth Advisers, LP and are subject to change without notice. Past performance is no guarantee for future results. This information is supplemental and complements a GIPS Report that can be found with composite performance. The securities referenced in the article are not a solicitation or recommendation to buy, sell or hold securities. This commentary is provided only for qualified and sophisticated institutional investors.

Results are presented gross and net of management fees and include the reinvestment of all income. The Net Returns are calculated based upon the highest published fees. The net performance has been reduced by the amount of the highest published fee that may be charged to SGA clients, 0.75%, employing the U.S. Large Cap Growth equity strategy during the period under consideration. Actual fees charged to clients may vary depending on, among other things, the applicable fees schedule and portfolio size. SGA's fees are available upon request and also may be found in Part 2A of its Form ADV. The performance record presented for periods prior to July 1, 2003 occurred before to the inception of SGA and represents the portable performance record established by two of SGA's founders (and investment committee members) Gordon Marchand and George Fraise while affiliated with a prior firm. The largest contributors and detractors are determined using a ranking of the absolute contribution to portfolio return by each security held over the period under consideration. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. Upon request, free of charge, SGA can provide a list of all portfolio holdings held in SGA's U.S. Large Cap Growth portfolio for the past year. SGA's earnings growth forecast data is based upon portfolio companies' non-GAAP operating earnings.

Sustainability Report

Q2 2022

SGA Sustainable Growth Advisers

Science-Based Targets Update

We renewed our commitment to support the proliferation of Science-Based Targets ("SBTs") in the corporate sector by once again lending our name as a signatory to CDP's annual letter campaign targeting the most climate-relevant companies within the global investable market yet to establish SBT commitments. Our primary avenue of engagement on material ESG issues such as the support of SBTs is direct engagement with company management teams. However, we welcome the opportunity for incremental advocacy by joining forces with peers when possible.

Regeneron

During the years we have owned shares in U.S. biotechnology company Regeneron, we have repeatedly advocated for stronger corporate governance at the firm. This quarter, we met with management for an update to our past engagement on matters of compensation and long-serving board members. Pleasingly, the company has made a number of changes recently in response to shareholder feedback, including ours. Regeneron will now hold an annual shareholder vote on compensation policies (previously held once every three years) which will give shareholders a greater voice in executive compensation policies. Furthermore, in response to concerns around long-serving board members, management indicated that we should expect to see new director nominations in the near-term, which again we believe will be beneficial to minority shareholders. We are of the opinion that current compensation policies for certain executives can be improved, and noted our concerns regarding the low hurdle rates for such rewards. We will continue to work with management to encourage and foster positive developments to the company's corporate governance.

Workday

We met with management of human resources software provider, Workday, over the quarter to share our suggestions to improve upon governance and compensation policies, and discuss specific proxy items.

On compensation, management acknowledged our concerns that share-based compensation is high relative to peers but maintains that the gap will narrow as hiring growth slows over the coming three years. We relayed our feedback that Short-Term Incentives (STIs) should be more performance-oriented and formulaic, as with peers such as Salesforce. Management responded that while STIs were designed to be discretionary in nature, they chose to more heavily feature stock rewards to drive stronger alignment. Regarding Long-Term Incentives (LTIs), we asserted that vesting of such awards should be performance-based and driven by total shareholder returns, rather than being solely time-based.

On the topic of governance, where Workday features a dual-class structure and anti-takeover defense mechanisms, there may be small incremental improvements to these structures such as last year's move to make majority-voting standard on Director elections. The Founders of the firm are intent upon preserving their control of Workday given the loss of their prior company to a hostile bidder. Management highlighted improvements in board refreshment and their strong diversity despite such governance structures.

On the re-election of board member Carl Eschenbach, which ISS opposed due to concerns about over-boarding, management made a spirited defense citing Carl's active involvement in the business. Management emphasized his ability to recruit key executives to Workday specifically because of his professional network and his involvement with other prominent technology company boards.

Lastly, on a recent proxy item, we voted against management on the Advisory Vote on Named Executive Officer (NEO) compensation. We believe the incentive plans are too discretionary and that the long-term incentive vesting should be performance-based, not time-based.

Proxy Voting Summary Q2 2022

	Number of Resolutions	For	%	Against	%	Abstain	%
U.S. Large Cap Growth	319	290	91%	29	9%	NIL	0%
Global Growth	342	322	94%	20	6%	NIL	0%
International Growth	317	305	96%	12	4%	NIL	0%
Emerging Markets Growth	159	141	89%	18	11%	NIL	0%
Global Mid-Cap Growth	285	272	95%	13	5%	NIL	0%

Source: SGA, ISS

Carbon Risks Q2 2022

	Total Carbon Emissions	Carbon Intensity	Weighted Average Carbon Intensity
SGA Global Growth	14,778	68.2	60.0
MSCI ACWI	88,951	187.6	169.2
SGA Relative Exposure	-83%	-64%	-65%
SGA U.S. Large Cap Growth	5,914	31.0	31.7
Russell 1000 Growth	15,068	67.5	52.9
SGA Relative Exposure	-61%	-54%	-40%
SGA Emerging Markets Growth	24,355	54.3	52.8
MSCI EM	250,545	404.7	326.5
SGA Relative Exposure	-90%	-87%	-84%
SGA International Growth	25,558	82.7	91.7
MSCI ACWI ex-USA	152,414	221.9	201.5
SGA Relative Exposure	-83%	-63%	-55%
SGA Global Mid Cap	15,187	58.6	47.5
MSCI ACWI Mid Cap	177,288	273.2	266.6
SGA Relative Exposure	-91%	-79%	-82%
	t CO_2e	t CO_2e / $M Sales	t CO_2e / $M Sales

Source: SGA, MSCI. Carbon data includes Scope 1 and 2 emissions.

SGA integrates ESG factors, including ESG risks and opportunities, into its investment process. SGA believes environmental, social and governance factors inherently impact a company's brand equity, employee satisfaction, competitive position, financial performance, and ultimately long-term shareholder value. Investments are made with the objective of maximizing risk-adjusted financial returns to its clients. SGA does not place a premium on social returns, nor does SGA allocate its clients' capital based on thematic or top-down views. The opinions expressed herein reflect the opinions of Sustainable Growth Advisers, LP and are subject to change without notice. The securities referenced in the article are not a solicitation or recommendation to buy, sell or hold securities. These materials are provided only for qualified and sophisticated institutional investors.