INVESTMENT REVIEW
4Q 2021

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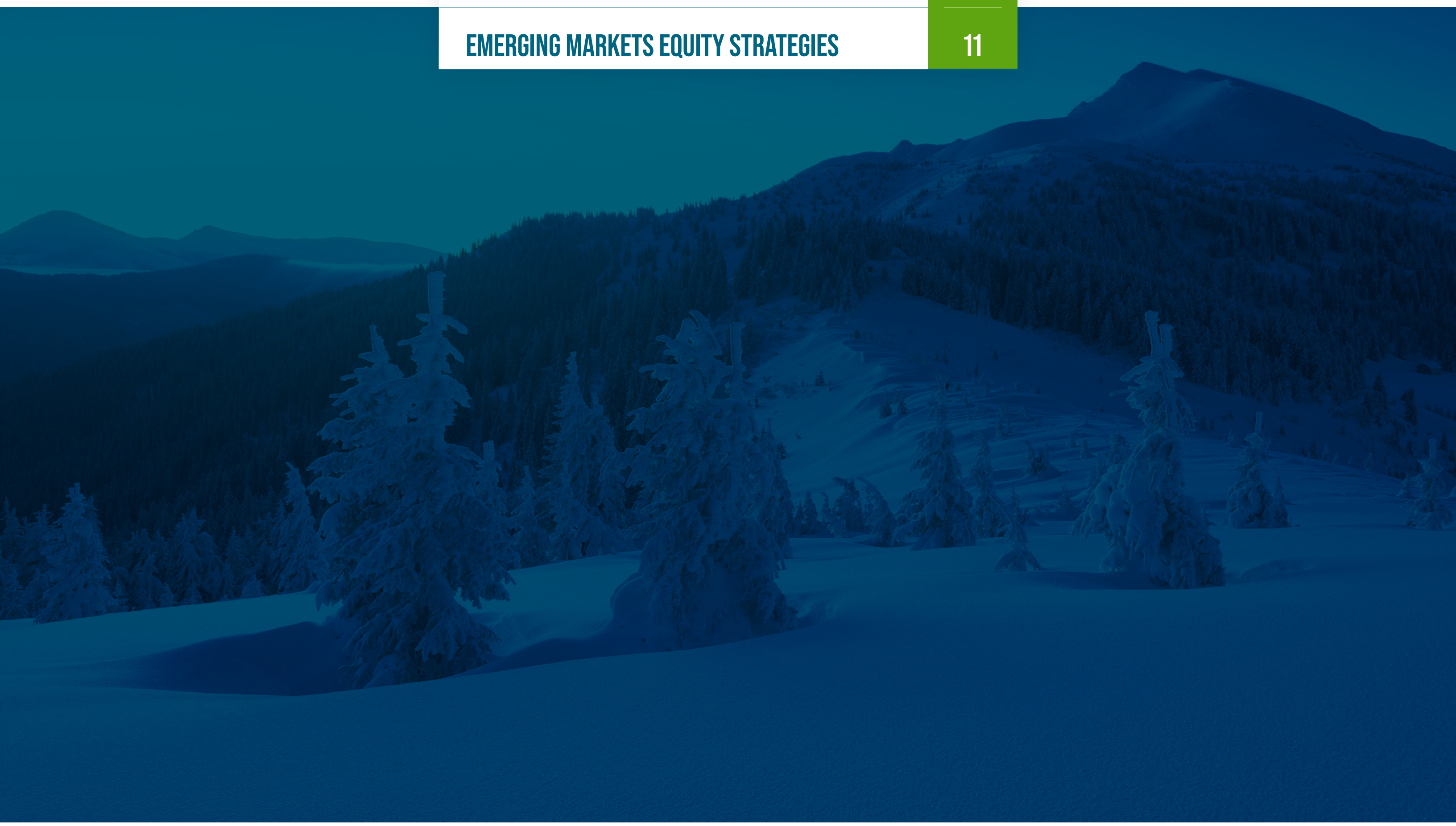

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ECONOMIC COMMENTARY

BY HAROLD G. KOTLER, CFA

Chief Executive Officer,
Chief Investment Officer

Are we going down a rabbit hole? Is the sky falling? Everywhere we look, the news seems daunting: new twists on the pandemic (Omicron), hyperinflation, Congressional stalemate, China's changing policies, Russia eyeing the Ukraine, rising interest rates, and Middle America, the so-called silent majority, frozen out by the extreme wings of both political parties.

It all sounds like the perfect setting for the next leg of a bull (yes, bull!) market. The fact is, equity investors prefer less-sweeping governmental policies and, given the state Washington is in, it's hard to expect that much more will be forthcoming. Moving into a mid-term election year, both parties need to move swing voters, which most likely means fewer compromises and a faltering Presidential agenda.

Omicron, like a wildfire, will burn itself out. Fast moving, less lethal, it may speed herd immunity. The various drug companies will have all sorts of treatments in 2022 and by mid-year the fear factor should be vastly lessened.

China does not want to experience what happened in Russia, i.e., a very few oligarchs in control of vast parts of their economy. Whether reigning in billionaires, making education affordable, limiting video game time for kids, or reducing excess speculation, it all seems reasonable to them. In a dictatorship, events are black or white, happen very quickly and are off-putting, especially to those in the developed world. China has no interest in being a democracy and does not play by the rules of the West. Its leadership wants to win an economic cold war, using the outside capital and ingenuity created by the West. The old saying holds true—the toothpaste is out of the tube. Their population wants the same economic benefits enjoyed in the West. They seem more than willing to trade what we call their "political voice" for security, education, health-care, and economic opportunity; that is the partnership Xi Jinping has contracted with the Chinese people. We in the West are unsettled by his abrupt policy changes, but he doesn't care what we think. China has had interference by foreign powers for more than 150 years. They will be their own system, owing nothing to anyone. It may be difficult to watch, but China will be the largest economy in the world in five years, so, like it or not, here they come.

Russia's barking at the West is more of the same. Of course they feel overwhelmed, since NATO, designed to offset the Soviet Union and all its puppet governments, has been pushed to their doorstep in an increasingly aggressive manner. We should stop this approach before unintended consequences emerge. The Biden administration's withdrawal from Afghanistan has called into question our resolve to stand by our allies, and hopefully Russia doesn't seize this moment as an opening to change the landscape of Europe.

> *"For years, I have likened our situation to Japan's, using a 10-year lag, and the comparison still holds. We are a mature economic system, with little immigration and a low birth rate. We depend on world trade and research to expand margins and create businesses."*

Next, the issue of the day—inflation. For as many years as I have written this piece I have said that inflation is not and will not be a problem. One might say that I have been right until this moment, but this time I'll be wrong. I still believe I am right; inflation is not and will not be a problem. If you are going to take the instance of a global pandemic leading to dislocations and extrapolate that into the future, you are going to be wrong. Of course prices have risen, either because businesses see the opportunity to take advantage of

Continued on next page

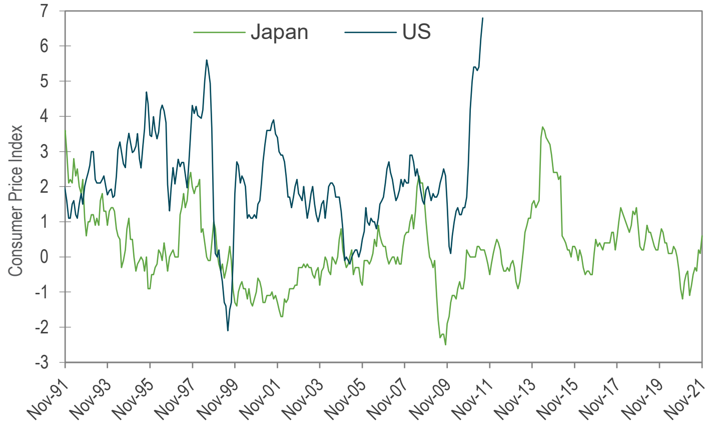
the times, or because there is a real reason, like the rising costs of labor and supplies. Either way, it makes little difference—in two years, when the supply chain normalizes and businesses get back to the new normal, there will be little room for price increases. The rising cost of labor is a healthy outcome. I don't see that as inflationary. Wages turn into consumption through sales, which sustain revenues. Even if companies lose a little in profit margins, it should not distress stock investors. The market wants a robust economy and the greater the degree of full-time workers and better wages, the better the economy will do.

Finally, fears about rising interest rates. While shorter rates will rise as central banks tighten monetary policy, long-term rates, which care only about inflation expectations, should remain more stable. Could the 10-year Treasury yield move from 1.48% to 2% or even 2.5%? Sure, so what? Rates will not move to 3% or 4%. If the government's cost of capital rises, then funding the deficit would crowd out discretionary spending. We are locked in a lower interest rate environment for a long time. For years, I have likened our situation to Japan's, using a 10-year lag, and the comparison still holds (Chart 1). We are a mature economic system, with little immigration and a low birth rate. We depend on world trade and research to expand margins and create businesses.

We will always be the leader in innovation and capital formation, but we need the world to buy our products, and the world needs us to buy theirs. This will be the key to peace—unequivocal mutual dependency. If the pandemic has taught us anything, it is that we all live on the same planet; we like to think that countries can operate independently to each other, controlling their own fate, but in a worldwide economy that's impossible. There are universal needs that nations mutually share, and the global economy will always reflect that.

CHART 1: U.S. vs. JAPAN INFLATION

Time Scale: Japan, U.S. lagged by 120 months



Comparison of U.S. and Japan CPI (Consumer Price Index). CPI percentages shown here are calculated on a rolling 12 month basis. U.S. data reflects the years 2003-2021 transposed over Japanese Date 1993-2011. Source: Bloomberg; Bureau of Labor Statistics. 120 month lag is the length of time between peaks in the Japanese and U.S. markets.

So don't worry. Get vaccinated. Live life and take advantage of those who see the world through dark glasses.

Harold G. Kotler, CFA

Chief Executive Officer, Chief Investment Officer

GW&K NEWS

GW&K RECOGNIZED AS A BEST PLACE TO WORK IN MONEY MANAGEMENT

Pensions&Investments BEST PLACES TO WORK IN MONEY MANAGEMENT ★★2021★★

Pensions & Investments, the global news source of money management, conducts this annual survey and recognition program to identify and recognize the best employers in the money management industry. We are proud to share the news, that as a first time participant, GW&K placed second in the 100-499 employee category.

Throughout our company's history we have nurtured a culture based on teamwork, integrity, trust and respect. We've always believed that people are our greatest asset, so to be recognized as a Best Place to Work in Money Management is an achievement of which we are very proud. Having an environment where people enjoy the work they do and feel supported, trusted and empowered, is critical to the success of GW&K. We believe that the highest levels of client service and employee productivity come from creating an environment of trust and respect.

We look forward to continued success and building long-term, mutually rewarding relationships with our clients, employees and broader community.

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41% EMPLOYEES WITH 10+ YEARS AT GW&K

$55 BILLION TOTAL ASSETS UNDER MANAGEMENT

FOURTH QUARTER 2021

ECONOMY

- The economy ended 2021 on a solid note, with strong household finances, rising employment and robust retail sales supporting an estimated 6% growth rate in Q4 according to a Bloomberg survey, a marked improvement from Q3 (2.3%).
- Inflation has also surged with the headline and core Consumer Price Indexes (CPI) for November up 6.8% and 4.9%, respectively from a year earlier. The headline CPI posted the highest rate of advance in 39 years.
- According to private-sector economic forecasts, inflation may take longer to return toward the Fed's 2% target than previously anticipated due to surging energy prices, ongoing supply-chain disruptions, and a tight labor market.

FED ACTION

- December's FOMC meeting formalized a hawkish pivot by the Fed as it doubled the pace of QE tapering, with the aim of ending its asset-purchase program by March.
- Policymakers also dropped their characterization of inflation as "transitory" and projected six quarter-point rate hikes over the course of 2022 and 2023.
- Fed funds futures have fully priced in three quarter-point rate hikes in 2022, with the first rate hike seen coming as early as the March FOMC meeting and no later than the May meeting.
- But futures markets project fewer out-year rate hikes than suggested by the Fed's official projections, reflecting the notion that more aggressive policy in the short run should successfully rein in price pressures over the longer term.

BOND MARKETS

- Fixed income markets were effectively flat in Q4, despite major narrative shifts with respect to inflation, monetary policy, and COVID-19.
- Treasuries posted a small gain, but not enough to reverse a decisive negative return for the full year, the first annual loss for the sector since 2013. The yield curve experienced a significant flattening as it became clear that the Fed no longer regards inflation as "transitory" and plans to act to cool it down.
- Corporates experienced a minor bout of volatility as heavy news flow whipsawed investor sentiment, though much of the weakness could be attributed to technical factors. New issuance maintained a brisk pace even amid elevated rate volatility. Spreads widened slightly, but sit close to historically tight levels as credit fundamentals remain robust.
- Municipals outperformed most fixed income asset classes for the quarter and the year driven by record breaking fund flows and below average tax-exempt issuance.

INDEX PERFORMANCE 12/31/21

	QUARTER	YEAR TO DATE
Bloomberg 10-Year Municipal Bond Index	0.55%	0.96%
Bloomberg Aggregate Bond Index	0.01%	-1.54%
Bloomberg High Yield Index	0.71%	5.28%
Dow Jones Industrial Average	7.87%	20.95%
S&P 500 Index	11.03%	28.71%
Russell 2000 Index	2.14%	14.82%
MSCI EAFE Index	2.69%	11.26%
MSCI World Small Cap ex USA Index	0.39%	11.14%
MSCI World Index	7.77%	21.82%
MSCI Emerging Markets Index	-1.31%	-2.54%

DOMESTIC EQUITY MARKETS

- U.S. equity markets closed Q4 sharply higher, capping a third consecutive year of double-digit gains for the S&P 500. Solid consumer demand and strong corporate earnings growth fueled the market's rise, overwhelming concerns around the Omicron variant, inflation, and prospects for rising interest rates in 2022.
- Large-cap stocks markedly outpaced small and mid-caps for the quarter and full year.
- Real Estate, Information Technology, Materials, and the Consumer groups were among the best performing sectors. Financials, Energy, and Industrials lagged on a relative basis for the quarter.
- Growth stocks outperformed Value in the large-cap Indexes, though Value maintained leadership over Growth in the small-cap market. Investors also demonstrated a preference for high-quality factors.

GLOBAL EQUITY MARKETS

- Non-U.S. developed markets (DM) advanced in Q4, led by Northern Europe, Canada, and Australia. The MSCI World ex USA Index gained 3.1%, finishing 2021 near record levels.
- DM small cap equities struggled to keep pace – the MSCI World Small Cap ex USA Index rose 0.4%. The U.S. Dollar rallied 1.8%.
- Ongoing weakness in Index heavyweight China (34% avg. weight) saw emerging market equities (EM) post a second consecutive quarterly decline. The MSCI Emerging Markets Index dropped -1.3%, though Taiwan and Southeast Asian markets posted strong returns.
- Semiconductors drove gains in EM Information Technology. EM Health Care and Consumer Discretionary were key detractors. DM Real Estate and Materials were among the sector leaders, while Health Care, Consumer Staples, and Communication Services underperformed.

INVESTMENT STRATEGIES

DOMESTIC EQUITY

We develop a deep understanding of the companies in which we invest through disciplined and intensive fundamental research. Our focus is on finding well-managed, quality companies, which are resilient.

GLOBAL EQUITY

We take advantage of market inefficiencies to find quality growth companies that may be undervalued, underappreciated, or under-researched. Our rigorous, bottom-up process focuses on a company's upside potential and downside risk.

TAXABLE BOND

Our multi-sector approach takes advantage of the relative valuation among distinct bond sectors and the increased opportunities to generate income and capital appreciation. We build diversified yield advantaged portfolios that generate steady, incremental income and provide downside risk protection.

MUNICIPAL BOND

We combine a rigorous, research intensive, credit selection process with active management. Our goal is to take advantage of market inefficiencies and find opportunities across the yield curve to protect and grow principal and income.

MUNICIPAL BOND STRATEGIES

Municipal bonds posted mixed returns in the fourth quarter—short maturities barely broke even, held back by the potential for an accelerated rate-hike cycle, while the long end rallied on declining growth expectations. Municipal bonds outperformed Treasuries across the entire curve, buoyed by a strong technical environment that had been in place all year. The broader market, meanwhile, experienced its second major selloff of 2021, though most of the losses were likewise concentrated at the short end, while the long end saw solid gains. Back in the first quarter, recall, the long end had led the slide, as investors repositioned during the so-called "reflation trade." This time around, the results reflected a market trying to juggle elevated growth and inflation against tighter monetary policy, less fiscal stimulus and the dampening effects of the Omicron variant. With inflation topping 30-year highs, the Fed executed a well-telegraphed hawkish pivot, doubling the pace of its expected taper and signaling as many as six quarter-point rate hikes over the next two years. The "transitory" moniker was also dropped from the policy statement, a nod to the reality that the spike in price increases is expected to linger far longer than originally anticipated. While two-year rates jumped 45 basis points over the quarter in reaction to the new messaging, 10-year rates were essentially unchanged. Whereas the 30-year rallied 14 basis points, an indication that investors believe the Fed will either succeed in keeping inflation at bay or damage the economy in trying.

Municipals charted their own path throughout the fourth quarter, largely ignoring the volatility in the Treasury market. After a brief hiccup in October, the market regained its footing in November and December. The catalyst was a seasonal boost in reinvestment flows against a backdrop of stable to falling issuance. In Washington, the House passed a version of the Build Back Better legislation, but left out key provisions that the municipal bond market lobbied hard for, including one that would have restored tax-exempt advanced refunding transactions. With that provision off the table, it seemed clear that the scarcity premium enjoyed by tax-exempt paper would persist further, an impression reinforced by the subsequent rally in municipals even while the Treasury market was in the midst of a pre-Thanksgiving Day slide. Meanwhile, the fundamental momentum remained intact. In November, Congress finally passed the bipartisan infrastructure bill, shoring up existing funding commitments and adding new federal grants to be used by all levels of government. Tax receipts continued to pour into state and local coffers, while outsized stock market gains helped bolster the funded status of pension systems across the board. For the quarter, the municipal curve mimicked the flattening of the Treasury curve, though short tax-exempt rates were up far less than their taxable counterparts, while longer-term yields fell by more. Those dynamics capped a year of outperformance that enabled municipals to stand as one of the few investment-grade fixed income sectors to post positive returns for 2021.

23 AVERAGE YEARS EXPERIENCE

14 MUNICIPAL INVESTMENT PROFESSIONALS

INVESTMENT TEAM

Nancy G. Angell, CFA	Partner, Co-Director of Fixed Income
John B. Fox, CFA	Partner, Co-Director of Fixed Income
Brian T. Moreland, CFA	Partner, Portfolio Manager
Martin R. Tourigny, CFA	Partner, Portfolio Manager

GW&K MUNICIPAL BOND STRATEGIES

- SHORT-TERM MUNICIPAL BOND
- 2–8 YEAR ACTIVE MUNICIPAL BOND
- 2–8 YEAR ACTIVE MUNICIPAL BOND ESG
- MUNICIPAL BOND
- MUNICIPAL BOND ESG
- MUNICIPAL ENHANCED YIELD

"Backed by unprecedented federal support, conservative budgeting and its status as one of the few high-quality tax shelters, municipal bonds are in good shape to weather any repricing in the broader markets."

From both a technical and fundamental perspective, the municipal bond market enters 2022 on a solid footing. The biggest questions moving forward involve valuation and the pace of improvement from here. After a year that saw a record $100 billion pour into industry mutual funds, it's hard to envision a material increase in retail demand. The same can be said for credit spreads, which blew out dramatically during the early days of the lockdown but have since rallied back to post-2007 tights. Even nominal rates, though well above the historical lows reached in the summer of 2020, begin the year at levels that would have been all-time lows before the onset of the pandemic. The resilience of municipal bonds in the face of broader weakness has left relative value ratios nearly two standard deviations rich to their long-term averages. And yet, the case for municipals remains compelling when you consider where we are in the market cycle. With asset valuations at record highs, investors would be well advised to remember the low correlation of municipal bonds with riskier securities, like equities, commodities, real estate and high yield. Backed by unprecedented federal support, conservative budgeting and its status as one of the few high-quality tax shelters, municipal bonds are in good shape to weather any repricing in the broader markets. To be sure, investors are currently paying a meaningful premium for such an attractive and reliable haven, but with few things as valuable as sleeping well at night, that shouldn't come as much of a surprise.

TAXABLE BOND STRATEGIES

20 AVERAGE YEARS EXPERIENCE

15 TAXABLE INVESTMENT PROFESSIONALS

INVESTMENT TEAM

Mary F. Kane, CFA	Partner, Portfolio Manager
Stephen J. Repoff, CFA	Principal, Portfolio Manager
Nancy G. Angell, CFA	Partner, Co-Director of Fixed
John B. Fox, CFA	Partner, Co-Director of Fixed

GW&K TAXABLE BOND STRATEGIES

- SHORT-TERM MUNICIPAL BOND
- INTERMEDIATE TAXABLE BOND
- CORE BOND
- CORE BOND ESG
- ENHANCED CORE BOND
- ENHANCED CORE BOND ESG
- TOTAL RETURN BOND
- CORPORATE BOND OPPORTUNITIES
- SHORT-TERM FOCUSED HIGH INCOME

"In light of our constructive fundamental outlook for the credit market and still-supportive market technicals, we believe the corporate credit space offers attractive value. Additionally, with Treasury rates at historically low levels, corporates offer a competitive yield and the potential for spread compression in a rising-rate environment."

Fixed income markets were effectively flat in the fourth quarter, despite major narrative shifts with respect to inflation, monetary policy, and COVID-19. Signs of easing supply-chain pressures and continued labor market normalization were not enough to quell concerns about rising inflation, which printed at its highest level in almost 40 years. The Fed executed a "hawkish pivot" in acknowledging more persistent inflationary forces and signaled their intention to respond accordingly. The extremely contagious Omicron variant rapidly established itself as the dominant strain around the globe, forcing a reappraisal of reopening timelines and reviving the specter of lockdowns and healthcare rationing. Ironically, the combined effect of these various forces essentially netted to zero; solid economic data and a broadly constructive outlook from the Fed were met with the prospect of tightening financial conditions and growth fears posed by omicron. But trading overall was orderly, and after the last two years investors seemed well practiced at looking past near-term volatility toward the next stage of a return to normalcy.

Treasuries posted a small gain, but it was not nearly enough to avert the first annual loss for the sector since 2013. The yield curve experienced a significant flattening as it became clear that the Fed no longer regards inflation as a "transitory" phenomenon and plans to act aggressively to cool it down. At their final meeting of the year, the FOMC announced an accelerated pace of tapering and projected an additional two hikes in 2022. Consequently, rates at the front end jumped to their highest level since prior to the pandemic, while long rates pushed lower despite slightly higher inflation expectations on weaker growth estimates. The revised dot plot finally aligned the central bank's projections with market expectations for 2022. Mortgage-backed securities underperformed Treasuries as a result of a deteriorating technical backdrop. The accelerated pace of tapering and uncertainty around reinvestments weighed on MBS spreads, though this was partially offset by a seasonal slowdown in originations and higher mortgage rates.

Corporates experienced a minor bout of volatility as heavy news flow whipsawed investor sentiment, though much of the weakness could be attributed to technical factors. New issuance maintained a brisk pace even amid a backdrop of elevated rate volatility. Spreads widened slightly but nevertheless sit close to historically tight levels as credit fundamentals remain robust. Measures of financial distress are scarce and the default rates sit well below long-term averages. Companies have been disciplined in their financial policies, especially in the more cyclical and capital-intensive sectors, where excess cash flows have been directed toward debt repayment. Companies have taken full advantage of capital market access to lower interest expenses and extend maturity schedules, thereby reducing both the likelihood and severity of credit market distress.

The meaningful shift in the Fed's reaction function—in addition to potentially elevated inflation pressure in the near term—suggest front-end maturities could face a challenging 2022. Farther out the curve, however, the outlook is less clear. With the Fed projecting a terminal rate near 2.5% and the market pricing in a ceiling closer to 1.75%, any fluctuation in this differential is likely to impact longer maturities most acutely as investors weigh the potential for a policy error. With respect to curve positioning, we think risks are fairly balanced.

In light of our constructive fundamental outlook for the credit market and still-supportive market technicals, we believe the corporate credit space offers attractive value. Additionally, with Treasury rates at historically low levels, corporates offer a competitive yield and the potential for spread compression in a rising-rate environment. While we are on guard against the potential for elevated M&A and an increased focus on shareholder returns, we see value in credit improvement stories within the investment grade space. In high yield, we favor crossover stories trading wide of investment grade peers while avoiding some of the more cyclical industries where we think good news is already reflected in spreads. We remain neutral on mortgages heading into the taper, though higher mortgage rates could improve our outlook for prepayment speeds. We also maintain our preference for higher-coupon, seasoned pools given our expectation of higher rates, as they are less exposed to extension risk.

DOMESTIC EQUITY STRATEGIES

23 AVERAGE YEARS EXPERIENCE

13 EQUITY INVESTMENT PROFESSIONALS

Year two of the COVID-19 pandemic proved to be a banner one for equity markets, as fiscal and monetary stimulus combined with successful vaccine introductions and strong economic growth pushed corporate earnings up to record levels. While the late-year emergence of the Omicron variant spooked the market post-Thanksgiving, those concerns abated and the market once again advanced to record highs late in the quarter.

The U.S. stock market, as measured by the S&P 500 Index, posted its best quarter of the year, advancing 11.0%, capping off an impressive full-year gain of 28.7%. Nearly all sectors showed positive returns in the quarter, led by the bond-proxy Real Estate sector and the mega-cap heavy Information Technology sector which both climbed by over 16%. Communication Services and Financials lagged in the quarter, as large media and entertainment stocks and banks struggled. Full-year returns were led by Energy, riding the 50% gain in crude oil prices, and Real Estate, whose high yields proved attractive to income-oriented investors. More defensive Utilities and Consumer Staples sectors lagged, as they often do in a bull market, as did Industrials, which suffered from supply-chain constraints and inflationary pressures.

Small cap stocks as measured by the Russell 2000 Index posted positive, but more modest gains of 2.1% in the quarter and 14.8% for the year. Unlike large caps, which posted more consistent gains all year, smaller caps peaked in March and then went sideways for the remainder of the year. The Communication Services and Health Care sectors dropped about -10% in the quarter, reflecting the less speculative nature of the quarter's returns as evidenced by large declines in meme stock AMC Entertainment and in the Biopharma industry. More defensive sectors, Utilities and Real estate posted double-digit gains. For the full year, Biopharma's mid-20% drop gave Health Care the distinction of being the only sector to post a decline for the year. In fact, its -16% decline was 30% worse than the next closest sector. Energy led the way for the year, up over 67%, as the less seasoned small cap companies in this sector continued to post a substantial turnaround from last year's near-death experience.

Large cap's strong fourth quarter further extended its lead over small caps, as the quarter's 8.9% relative performance extended the full year advantage to 13.9%. This relative strength can be attributed to the exceptional performance of the mega-cap names in the Information Technology and Consumer Discretionary sectors, as well as extreme weakness among small cap non-earners, especially Biopharma and Software names.

Among large cap stocks, Growth was clearly in favor in the quarter, driven by broad strength in the Information Technology sector. This surge pushed Growth ahead of Value for the year as well, although the modest two point spread was tempered somewhat by strong performance in the value-oriented Financials sector. Small cap leadership was just the opposite, as the disastrous performance by growth stocks in the Health Care sector explains most of Growth's underperformance versus Value in both the quarter and the year. In fact, small cap Value's 25% performance advantage over Growth was its largest since the Internet bubble burst in 2000.

We remain generally positive in our outlook toward equities entering 2022. This is not to say there are not risks. The Omicron variant clearly creates threats, especially to consumer demand and in supply-chain disruption. But thankfully the evidence points to a less dangerous, albeit highly contagious, variant that may very well be peaking out in the next few weeks. While not likely to be resolved immediately, supply-chain disruption should slowly but surely dissipate as the year progresses. Fed tapering is also cited as a risk to the 2022 outlook, as interest rates will likely climb and demand for risk assets may fall as accommodative monetary policies of the past two years are reversed. However, the strength of the economy should be sufficient to overcome these pressures. Favorable wage and unemployment statistics, strong housing prices and demand, solid Consumer spending and expansionary ISM Manufacturing and Services surveys, to name but a few, all still point to sustained economic growth. Lastly, inflation is proving to be less transient than initially expected. Indeed, inflation rates are hitting multi-decade highs. Certain components of inflation such as wage rates and housing do feel more persistent, although other components of inflation should be tempered by the easing of supply-chain constraints.

INVESTMENT TEAM

Daniel L. Miller, CFA	Partner, Director of Equities
Joseph C. Craigen, CFA	Partner, Portfolio Manager
Jeffrey W. Thibault, CFA	Partner, Portfolio Manager
Jeffrey O. Whitney, CFA	Partner, Portfolio Manager
Aaron C. Clark, CFA	Principal, Portfolio Manager

GW&K DOMESTIC EQUITY STRATEGIES

- EQUITY DIVIDEND PLUS
- DIVERSIFIED EQUITY
- SMALL/MID CAP CORE
- SMALL/MID CAP GROWTH
- SMALL CAP VALUE
- SMALL CAP CORE
- SMALL CAP GROWTH

> *"Our confidence is high that the economy will return to solid footing as the pandemic comes to an end, hopefully around mid-year."*

GLOBAL EQUITY STRATEGIES

24 AVERAGE YEARS EXPERIENCE

8 EQUITY INVESTMENT PROFESSIONALS

INVESTMENT TEAM

Daniel L. Miller, CFA	Partner, Director of Equities
Reid T. Galas, CFA	Partner, Portfolio Manager
Karl M. Kyriss, CFA	Partner, Portfolio Manager

GW&K GLOBAL EQUITY STRATEGIES

GLOBAL SMALL CAP

INTERNATIONAL SMALL CAP

"...the year ahead is likely to be just as full of risk as opportunity. The expected monetary tightening in the U.S., happening just as we approach a potential fiscal cliff caused by an end to pandemic-era stimulus spending, could prove to be a very bearish combination...With so much happening we think the best approach is to focus on bottom-up stock picking with a quality bias."

Global developed markets finished the year higher with the MSCI World ex USA and MSCI World ex USA Small Cap Indexes up 3.1% and 0.4% for the quarter, and 12.6% and 11.1% for the year, respectively. The local returns were much stronger than they appeared as renewed USD strength subtracted about 1.1% for the quarter and 6.5% for the year when translating back from foreign currencies to the U.S. dollar.

It was difficult to draw any macro conclusions from results this quarter. On a sector basis Real Estate, Materials, and Utilities had the best returns, while Consumer Staples, Health Care, and Communication Services sold off. Geographically, both Europe and North America had positive returns, but Asia fell on weakness in Japan and Hong Kong. The yen weakened through a trading range that has held for five years. Historically a weak yen has been supportive of the equity markets, but that correlation did not hold true this quarter. The best markets during the quarter were mostly outside of Asia with a strong rally in Israel, the Nordics, and Australia.

The fourth quarter felt like an intermission prior to COVID-19's final act. We expect a tentative start to 2022 and then an accelerating recovery in Asia and Europe. Apart from China, and to some extent Japan, most governments have moved towards treating COVID-19 as endemic, and as a result restrictions on travel and services should ease. Global supply chains will also improve although some issues will persist. In particular, we expect a significant improvement in the auto industry. The industry continues to see strong demand but has been unable to fully capitalize as production constraints and lean inventories depress sales. High prices have offset the impact on the Original Equipment Manufacturers (OEMs), but many suppliers are suffering from low production levels. As supply issues resolve and production ramps up, the impact across the supply chain will provide a strong tailwind for global expansion. At the same time, industrial capital expenditures should continue to be strong as companies invest to offset labor shortages and reshape supply chains. If services demand also picks up and global travel resumes the international markets should see a growth catch-up boost to rival what has already occurred in the U.S.

Unfortunately, the year ahead is likely to be just as full of risk as opportunity. The expected monetary tightening in the U.S., happening just as we approach a potential fiscal cliff caused by an end to pandemic-era stimulus spending, could prove to be a very bearish combination. If the Fed is successful in raising rates they may find demand is more sensitive than expected to monthly payment terms, causing a sharp slowdown in spending.

Political risks are also increasing, both long term and short. In Europe, the risk of a Russian "annexation" of Eastern Ukraine grows and the West's response will likely be an important input into China's future strategy towards Taiwan. In Asia, Xi will be focused on securing his third term as General Secretary and potentially Party Chairman. Meanwhile, Japan begins rearming for the first time since World War II. In the Middle East, the long-running Iranian nuclear program drama potentially reaches a climax.

One frustration in 2021 was our view that there was a disconnect between the underlying fundamental results at a company level and the market's recognition of those results. We tend to think changes in portfolio fundamentals that exceed the market returns as compressing a spring. Eventually the spring is sprung and fundamentals will win out.

With so much happening we think the best approach is to focus on bottom-up stock picking with a quality bias. The four key portfolio metrics to focus on are: faster projected growth, lower valuation, better return metrics, and stronger balance sheets than the Index. It is difficult to find all four characteristics in any individual company, but this mixture should be attainable at the portfolio level. Over the long term, we expect that combination of characteristics should result in attractive relative returns, but sometimes patience is required. This is representative of how we invest, with eyes on both risks and opportunities and a focus on long-term company specific fundamentals.

EMERGING MARKETS EQUITY STRATEGIES

28 AVERAGE YEARS EXPERIENCE

18 EQUITY INVESTMENT PROFESSIONALS

INVESTMENT TEAM

Daniel L. Miller, CFA	Partner, Director of Equities
Nuno Fernandes, CFA	Partner, Portfolio Manager
Thomas A. Masi, CFA	Partner, Portfolio Manager
Bradley J. Miller, CFA	Partner, Portfolio Manager
Pablo Salas	Partner, Portfolio Manager
William P. Sterling, Ph.D.	Global Strategist

GW&K EMERGING MARKETS EQUITY STRATEGIES

EMERGING MARKETS EQUITY

EMERGING WEALTH EQUITY

Emerging market (EM) equities capped off a disappointing year with the MSCI EM Index declining -1.3% for the quarter and -2.5% for the year. In comparison, the MSCI World Index of developed market (DM) equities gained 7.8% for the quarter and 21.8% for the year. Last year marked the most pronounced annual underperformance of EM equities versus DM equities since the "taper-tantrum" year of 2013. EM's fourth-quarter underperformance reflected some of the same factors that hindered its full-year performance, including China's ongoing market and economic malaise, global supply-chain stresses associated with the pandemic, the Fed's increasingly hawkish posture, elevated energy prices, and a spree of rate hikes by EM central banks.

With MSCI China representing about one-third of the MSCI EM Index, its recent weakness has masked decent performance of other EM equity markets. For example, in the quarter, MSCI EM ex-China was up 1.1% while China posted a loss of -6.1%. For 2021 overall, MSCI EM ex-China posted a gain of 10.0%, while China posted a loss of -21.7%. Headwinds for Chinese equities in recent quarters have included multiple regulatory clampdowns associated with President Xi's "common prosperity" program, a severe property market credit crunch, and disappointing economic performance associated with rolling COVID-19 lockdowns and production cutbacks.

EM's modest decline in the quarter was associated with widespread weakness across sectors. Only two EM sectors, Information Technology and Utilities, posted positive performance for the quarter, with gains of 7.4% and 0.7% respectively. The weakest EM sectors in the quarter were Consumer Discretionary, Real Estate, and Health Care, with respective losses of -8.2%, -8.5%, and -15.3%. On a full-year basis, the MSCI EM Index's modest loss of -2.5% masked a wide dispersion of sector performance. Energy, Utilities, and Information Technology posted double-digit gains for the year, while Health Care, Real Estate, and Consumer Discretionary posted double-digit losses. The large Consumer Discretionary sector was notably weak, with a loss of -29.1% for the year reflecting China's regulatory clampdown and more general EM margin pressures associated with higher energy and other input prices.

As is often the case in EM, there was a wide dispersion of returns among countries and regions in both the quarter and year overall. In the quarter, the Czech Republic, Egypt, Peru, and the United Arab Emirates posted double-digit gains, while Chile and Turkey posted double-digit declines. For 2021 overall, the Czech Republic, the United Arab Emirates, and Saudi Arabia posted gains exceeding 40%, while other standout performers were Argentina, India, Mexico, and Taiwan, with gains in the 20-30% range. In contrast, China, Pakistan, and Turkey posted full-year losses exceeding -20%. For the year, regional returns were also widely dispersed with the EM region of Europe, the Middle East, and Africa (EMEA) posting a gain of 23.9% while EM Asia and EM Latin America posted declines of -5.1% and -8.1%, respectively. The notable full-year performance of the EMEA region reflected improved prospects for energy-exporting nations in a year when the price of Brent crude oil rose by 53%.

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Looking back, EM nations clearly participated in the global economic recovery in 2021, with Bloomberg's estimates of 12-month forward profits rising by 45.5% over the course of the year. However, the MSCI EM Index failed to participate in the global equity rally because the forward P/E multiple fell sharply from 19.0x to 12.4x over the same period. With the benefit of hindsight, China's regulatory clampdown and a spree of rate hikes by EM central banks outside of China seemed to be the main factors depressing EM valuation multiples in 2021.

With the MSCI EM Index now trading at a modest forward multiple of 11.9x and with analysts projecting EPS growth of 17% for 2022 and 10% for 2023, the outlook for EM equities looks reasonably constructive. It is encouraging that Chinese policymakers have pivoted toward more growth-friendly policy in recent weeks and that the worst of the regulatory clampdown appears to be in the rear-view mirror. To be sure, risks remain including prospects for Fed tightening and those associated with the rise of the Omicron variant. On the positive side, these risks seem well discounted in last year's EM multiple contraction, while any positive developments like an early peaking of the Omicron wave or more constructive regulatory news from China could help EM equity valuation multiples stabilize or even improve in the year ahead.

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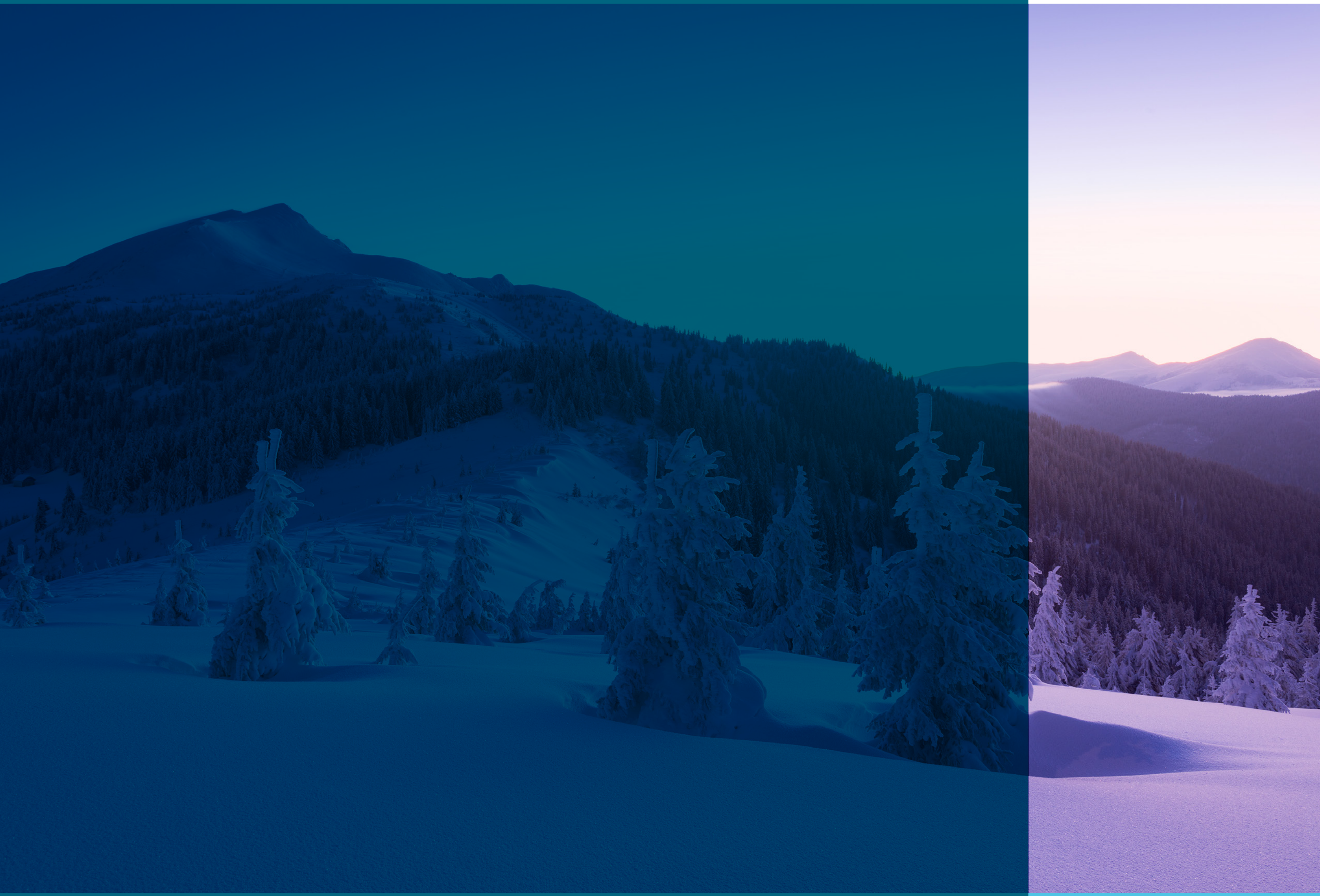

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