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INVESTMENT STRATEGY OUTLOOK – SMALL CAP EQUITY

June 30, 2016

The FMI Small Cap portfolios returned approximately 1.1% in the June quarter compared to 3.79% for the Russell 2000 Index. Sectors that outperformed included Transportation, Technology Services and Consumer Services, while laggards included Commercial Services, Distribution Services and Health Technology. Stocks that helped relative performance included Kirby, Woodward and Cable One, while ManpowerGroup, MSC Industrial and Arrow Electronics underperformed. The portfolios, being value-oriented, have performed about as expected over the course of this bull market, which is to say they have slightly lagged the growth-oriented benchmark, and have performed roughly in line with the Russell 2000. Heavy flows coming out of active management and going to passive index products have created a negative feedback loop for active participants and the opposite for passive. These things generally move in cycles and have reversed dramatically in the past two bear markets. While the current cycle is particularly long, we are confident the same general pattern will occur. We've already seen a glimpse of this in the international arena, where over the past twelve months the MSCI EAFE index (local currency) is down -10.19% while the FMI International portfolios are up approximately 1.7%. The same phenomenon has transpired to a somewhat lesser degree in the FMI Small Cap portfolios, where performance is down approximately -0.5% over the trailing twelve months compared to a loss of 6.73% for the Russell 2000.

Investors running to passive strategies are engaging in another form of performance chasing. Any asset can become overvalued, leading to a disappointment and eventual underperformance. People have been trained to think in short-term time frames but sometimes cycles can last a very long time, as evidenced by the current one beginning in March of 2009. Memories are short in this business but it's healthy to be reminded of history. In the last bear market, which began in the fourth quarter of 2007, the average price-to-sales ratio of the S&P Industrials was approximately 1.5, which was quite high. Five quarters later this figure was below 0.9 and the total return of the S&P 500 was -55.0%. In the cycle before that, which peaked in March of 2000, the average price-to-sales ratio of the S&P Industrials was over 2.1. Ten quarters later the ratio was approximately 1.2, with the S&P 500 suffering a 47% negative total return. Today, the S&P Industrials trade at a price-to-sales ratio of approximately 1.7, compared to the 60-year median of slightly less than 1.0. High valuations have been around for so long that people's guards are down. Complacency is like a fog permeating the investment landscape. Investors convince themselves it will be different this time for a host of reasons, e.g., low interest rates, low inflation, equity scarcity, and an omniscient Federal Reserve.

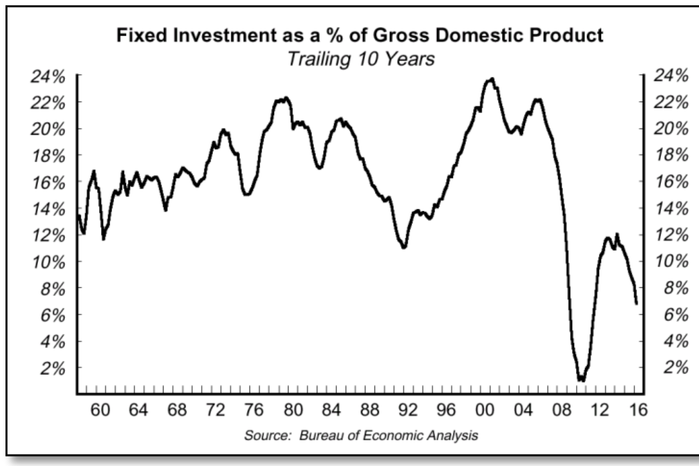
Today's market trades in the 8th decile (10th being the most expensive), based on the median of 50 valuation measures the Leuthold Group publishes. There are very few good companies that can be had at truly bargain prices. This makes the current cycle quite different than the last two, wherein it was not that difficult to build a cheap and adequately diversified portfolio despite the benchmarks trading at high valuations. Yes, it took great resolve to be contrarian and avoid a couple of highly-speculative and popular sectors or over-levered financials, but at least there were plenty of attractive alternatives. Today, investors face a difficult set of choices:

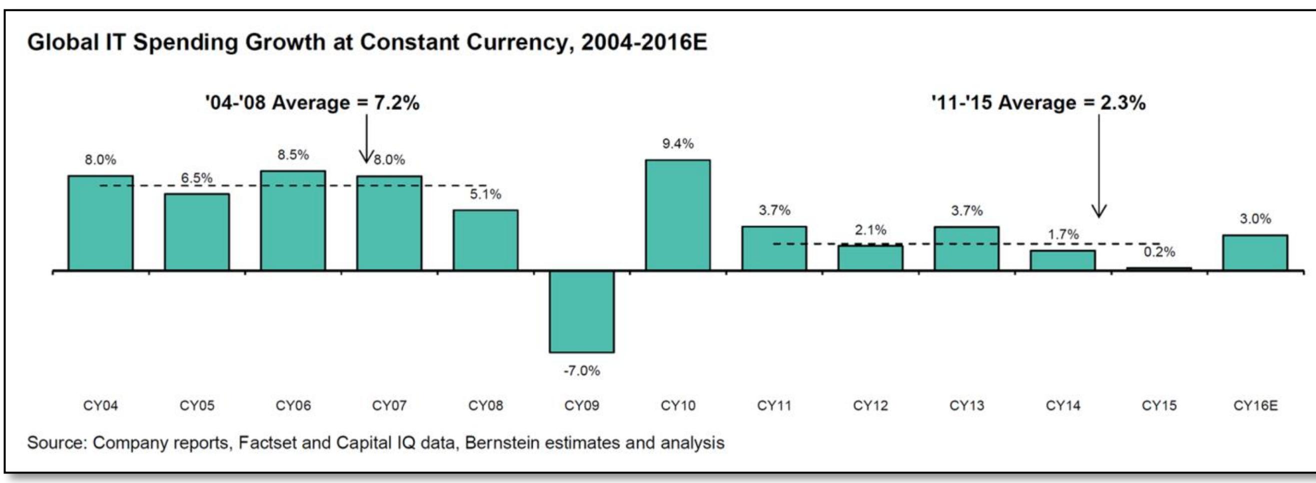
- Concede "defeat" to the index products and join the crowd.
- Invest in a few isolated opportunities, foregoing diversification.
- Carry a large amount of cash.
- Invest in a portfolio of good businesses that, while not cheap, trade at a very significant discount to the popular benchmarks.

We continue to choose the last option. Equity investing still trumps cash over the long run, but we anticipate a bumpy ride.

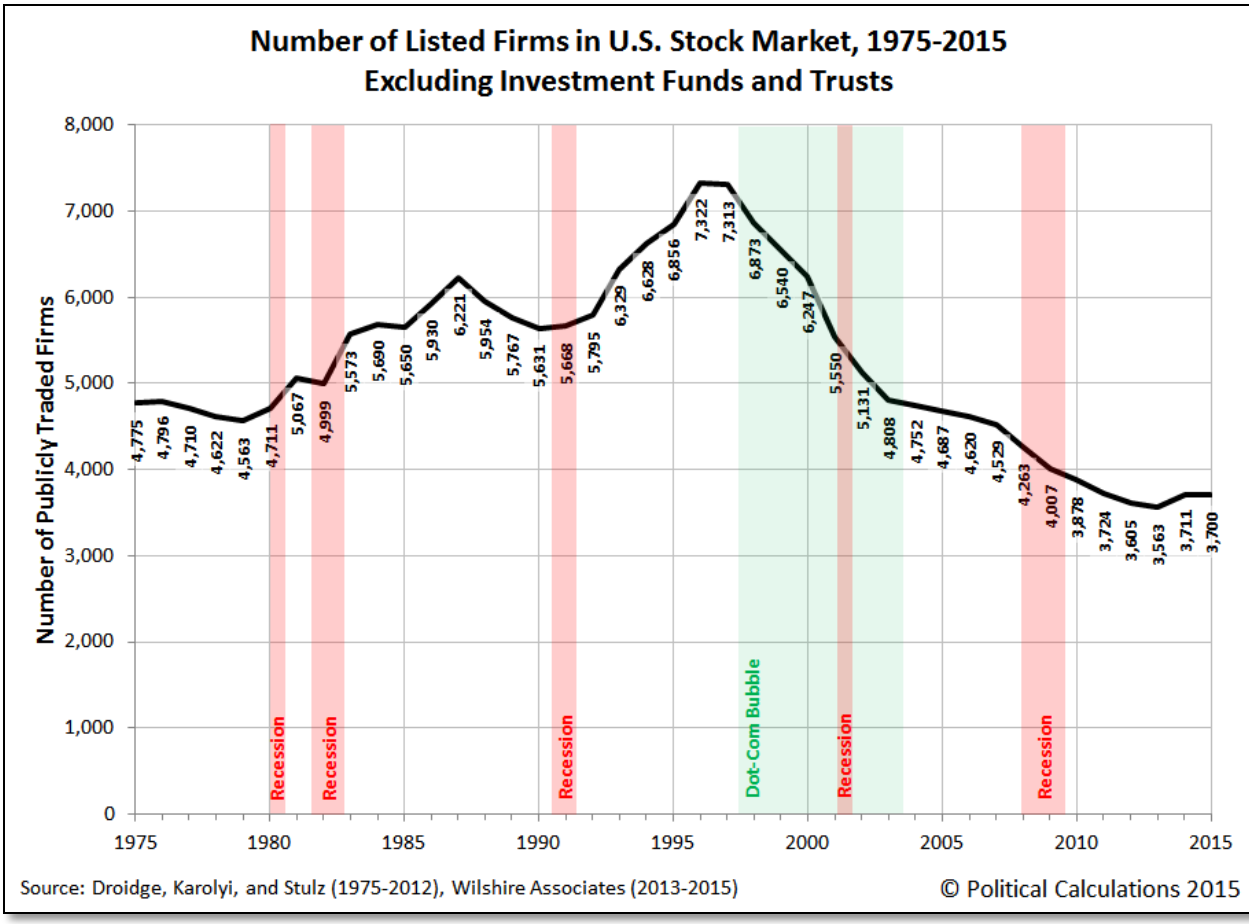
Since we start from a position of high valuations, it certainly does not seem likely that stocks can sustainably climb without fundamental improvements in sales and earnings. Both of these have been flat to down over the past twelve months for the S&P 500. Corporations have been pulling out all of the stops to keep earnings afloat, including engaging in massive earnings per share deception. The gap between reported earnings using generally accepted accounting principles (GAAP) and so-called "adjusted" earnings is cavernous. In the first quarter, there was a 29% difference between GAAP earnings and so-called "adjusted" earnings for the Dow Jones Industrial Average. According to a recent *Wall Street Journal* article, just 29 companies in the S&P 500 exclusively use GAAP earnings. It used to be only a handful of technology companies played this game; now it is almost ubiquitous.

With margins near historically high levels (though slipping), earnings are unlikely to improve until sales improve and that's going to be hard unless the economy improves. Here the story gets difficult. Real GDP has been essentially stuck in a 0-2% channel for a decade, averaging 1.4%. We haven't printed an annual growth rate above 3% since 2005 and recent performance has been anemic. We've posited for some time that organic growth is low because investment is low. Nearby are two charts, one for fixed business investment and the other for information technology (IT) spending, illustrating this point.





A few weeks ago the cover story for *Barron's* was "The Disappearing IPO [initial public offering]". The total number of public companies today is roughly half of what it was twenty years ago (see the following chart). Business confidence has been sub-par for years.



We think the increasing regulatory burden is a significant factor in the lack of business vitality over the past decade. The Code of Federal Regulations is up to 175,000 pages in 236 volumes. It contains over one million individual instructions that mandate or prohibit some activity. The Dodd Frank legislation, already the lengthiest ever, continues to expand as new rules are issued. What started as a 13,000 page behemoth is now 22,000 pages. In 2015, 114 new laws were enacted, while federal agencies issued 3,410 new regulations. Sixty federal agencies have over 3,000 regulations in the pipeline. The 2015 *Federal Register* contains 80,260 pages and 94,246 rules, up over 30% since 2008. The tax code is over 75,000 pages long and has grown significantly over the past decade. Businesses are choking on red tape and this is stifling new corporate formation and existing business expansion. It has particularly hurt the little guy, with difficult wage and total employment statistics. The so-called fourth branch of government (regulatory apparatus) has been emboldened by anti-business sentiment in Congress and the executive branch. The Competitive Enterprise Institute, in their annual survey,

estimates that the cost of these regulations is $1.88 trillion per year, approximately 10% of GDP and a hidden tax of $15,000 per U.S. household.

Nobody is foolish enough to suggest or imply that regulatory oversight is unnecessary. The cost and complexity of rules and regulations, however, has to be better balanced against the benefits. Bureaucrats, sometimes with political agendas, can wreak havoc on private enterprise. In our conversations with CEOs and CFOs, the overwhelming sentiment is that the government is out of control from a regulatory standpoint. The explosion in our public sector debt buttresses this case. Everyone needs to understand that healthy democratic capitalism is essential to the welfare of both private and public sectors. This economy needs a restart. Winston Churchill once said, “No matter how beautiful the strategy, you should occasionally look at the results.” We’ve tried fiscal stimulus; it hasn’t worked. We’ve tried almost nonstop accommodative monetary policy; it hasn’t worked. How about a roll-back and simplification of the regulatory state and a simplified tax code?

U.S. corporate tax rates are the highest among those in the Organisation for Economic Co-operation and Development (OECD). These taxes are based primarily on where the business is chartered rather than where the income is generated. Instead of demonizing corporations for seeking corporate inversions (acquiring an offshore company and changing the domicile), why not lower and simplify the tax rate? Instead of companies leaving the U.S., it might even attract new ones and it would motivate businesses to expand facilities and employment right here. A joint project between the Urban-Brookings Tax Policy Center and the American Enterprise Institute advocates cutting the federal corporate tax rate from 35% to 15%.

> “*Americans owning stock in publicly traded companies would be taxed at ordinary income tax rates on their dividends and capital gains. Capital gains on stocks would be taxed, and capital losses would be deducted, as they accrue, even if the stock had not been sold. American shareholders would be allowed to credit their share of companies’ corporate income tax payments against their dividend and capital gains taxes. These credits would not be provided to foreign shareholders or to tax-exempt shareholders (nonprofit organizations and retirement plans).”*

This proposal links tax liability more closely to where shareholders, who ultimately receive corporate profits, live. It is not ideal, but it is a compromise between the left and the right and it is a good start in simplifying the overall tax code, which we believe would be very beneficial to economic growth and the people’s prosperity.

Finally, late in the quarter the United Kingdom referendum to leave the European Union (EU) proved most of the polls and the bookies wrong. It rattled stock markets significantly. The overwhelming sentiment from the pundits is that “Brexit” is a negative. That may be true in the short run, but it’s important to consider the long term. Turn it around and ask “What has the EU done for its members over the past two decades?” Growth has been anemic. Debt has exploded. The number of employed, as a percentage of the working age population is abysmal. Taxes and regulations have grown significantly. Business vibrancy is low. Birth rates have plummeted. The ability to be a sovereign nation and control decisions on issues like immigration has been curtailed. The EU has been ineffective with respect to Putin. Of course, the issues are not black and white. European countries are not fighting each other as they did in the 1940s and common commerce standards have been a positive. Nevertheless, our long held belief, shared in these letters, is that it is nearly impossible to have a monetary union without a political union and we do not see a political union anytime soon. Practically speaking, it will be a few years before new treaties are signed and a lot can happen in the meantime in terms of restructuring and negotiating. Our strategy is to buy when there is the proverbial blood in the streets.

Thank you for your confidence in Fiduciary Management, Inc.

Fiduciary Management Inc.
Small Cap Equity Composite
12/31/2005 - 03/31/2016

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation Composite	Three Year Ex-Post Standard Deviation *Benchmark	Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
2006	18.46	17.56	18.37	147	0.73	n/a	n/a	$ 1,606.8	$ 3,589.4	44.77%
2007	-0.92	-1.72	-1.57	161	0.85	n/a	n/a	$ 1,520.2	$ 3,960.4	38.39%
2008	-21.06	-21.69	-33.79	145	1.16	n/a	n/a	$ 1,212.4	$ 4,062.5	29.84%
2009	35.72	34.56	27.17	165	0.97	n/a	n/a	$ 2,004.6	$ 7,008.9	28.60%
2010	23.45	22.43	26.85	170	0.48	n/a	n/a	$ 2,477.7	$ 9,816.0	25.24%
2011	5.64	4.79	-4.18	179	0.34	21.17%	24.99%	$ 2,523.2	$ 12,273.6	20.56%
2012	11.34	10.43	16.35	182	0.40	15.46%	20.20%	$ 2,609.5	$ 15,253.5	17.11%
2013	33.43	32.33	38.82	180	1.04	12.51%	16.45%	$ 2,801.8	$ 19,705.3	14.22%
2014	7.99	7.06	4.89	178	0.39	9.65%	13.12%	$ 3,006.5	$ 21,001.1	14.32%
2015	-5.72	-6.52	-4.41	171	0.34	11.18%	13.98%	$ 2,597.2	$ 21,042.9	12.34%
Q1 2016	5.77	5.55	-1.52	171	0.11	11.82%	15.13%	$ 2,587.8	$ 21,477.7	12.05%

*Benchmark: Russell 2000 Index®

Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Inc. (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 03/31/2016. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Small Cap Equity composite has been examined for the periods 12/31/1993 -03/31/2016. The verification and performance examination reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $21.4 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The FMI Small Cap Equity Composite was created in January 1980. These accounts primarily invest in small to medium capitalization US equities.

The FMI Small Cap Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts, with a market value greater than $500,000 as of month end. A small percentage of composite assets (typically ranging from 0-5%) historically has been invested in unmanaged fixed income securities at the direction of account holders. From December 31, 1993 thru September 30, 2002 all accounts included were managed for at least one quarter, from October 1, 2002 to present all accounts were managed for at least one month. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes. Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2011, the trailing three year annualized ex-post standard deviation for the Composite and Benchmark are required to be stated per GIPS®.

Currently, the advisory fee structure for the FMI Small Cap Equity Composite portfolios is as follows:

Up to $25,000,000	0.90%
$25,000,001-$50,000,000	0.85%
$50,000,001-$100,000,000	0.75%
$100,000,001 and above	0.65%

The firm generally requires a minimum of $3 million in assets to establish a discretionary account. High Net Worth individuals may establish an account with a minimum of $1,000,000, however, the firm reserves the right to charge a minimum dollar fee for High Net Worth individuals depending on the client servicing involved. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request.
Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The Russell 2000 Index® measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000® Index representing approximately 8% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. The Small Cap Equity composite uses the Russell 2000 Index® as its primary index comparison.

Fiduciary Management Inc.
International Equity Composite
12/31/2010 - 03/31/2016

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation Composite	Three Year Ex-Post Standard Deviation *Benchmark	Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
2011	-0.78	-1.52	-12.15	1	0.00	n/a	n/a	$ 16.7	$ 12,273.6	0.14%
2012	19.35	18.46	17.31	1	0.00	n/a	n/a	$ 76.3	$ 15,253.5	0.50%
2013	25.89	24.95	26.93	1	0.00	9.78	12.22	$ 165.8	$ 19,705.3	0.84%
2014	5.66	4.87	5.92	1	0.00	7.49	10.33	$ 771.6	$ 21,001.1	3.67%
2015	4.24	3.46	5.33	2	0.00	8.14	11.73	$ 2,832.9	$ 21,042.9	13.46%
Q1 2016	1.90	1.71	-6.52	2	0.12	8.01	11.96	$ 3,464.9	$ 21,477.7	16.13%

*MSCI EAFE Net Local Index®

Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Incorporated (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 03/31/2016. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The International Equity Composite has been examined for the periods 12/31/2010-03/31/2016. The verification and performance examination reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $21.4 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The International Equity Composite was created on December 31, 2010. This composite invests mainly in a limited number (usually between 25-35) of large capitalization (namely, companies with more than $5 billion market capitalization) foreign companies.

The International Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees, gross of custodial fees, gross of withholding taxes and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes. Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2011, the trailing three year annualized ex-post standard deviation for the Composite and Benchmark are required to be stated per GIPS®. For the periods 2011-2012, the information is not available for the International Equity Composite.

Currently, the advisory fee structure for the International Equity Composite portfolios is as follows:

Up to $25,000,000	0.70%
$25,000,001-$50,000,000	0.65%
$50,000,001-$100,000,000	0.60%
$100,000,001 and above	0.55%

The firm generally requires a minimum of $25 million in assets to establish a discretionary account. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The MSCI EAFE Net Local Index® is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Net Local Index consists of the following 21 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. It is reported in local currency and net of hedges. The International Equity composite uses the MSCI EAFE Net Local Index® as its primary index comparison.