

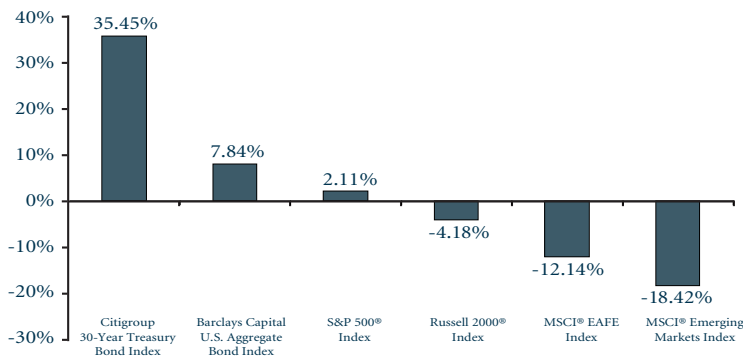


2011 — ANOTHER ROLLER COASTER YEAR FOR EQUITIES

Not unlike 2010, equity prices were extremely volatile throughout 2011. The first quarter and the fourth quarter generated positive equity returns. However, the second and third quarters were very challenging for both the economy and equity prices. Overall, the year finished about where it started with the S&P 500 Index up 2.11%. Growth (as measured by the Russell 1000 Growth Index) gained 2.64% for the year and outperformed value (as measured by the Russell 1000 Value Index), which returned 0.39%, due to continued weakness in the financial sector which constitutes a large portion of the value index. Small stocks, as measured by the Russell 2000 Index, and emerging-market stocks, as measured by the MSCI Emerging Markets Index, declined 4.18% and 18.42%, respectively, in 2011 due to global recession fears triggered by the European Sovereign Debt Crisis. Similar to 2008, U.S. Treasury bonds were the best performing asset class in 2011 (the Citigroup 30-Year Treasury Bond Index was up 35.45% for the year) despite the downgrade of U.S. debt as global slowdown fears intensified throughout the year. Although not as strong as the return of U.S. Treasuries, the Barclays Capital U.S. Aggregate Bond Index also had a positive year with a 7.84% return for the period.

INDEX RETURNS

ONE YEAR ENDING DECEMBER 31, 2011



Source: FactSet Research Systems

Data is assumed to be reliable. Past performance is no guarantee of future results.

Ironically, a strong consensus among professional investors coming into 2011 was that rising input costs from overseas labor and rapidly rising commodity prices would cause significant inflation. Therefore, common advice was that investors should avoid Treasury bond and fixed-income vehicles as yields would surely rise from their low levels. Additionally, the European debt crisis seemed well contained to Portugal, Ireland, and Greece. Through the end of the first quarter, this scenario seemed to be playing out in financial markets. Yet, by the end of the first quarter, cracks started to appear in the global growth/inflation story.

As the second quarter unfolded, Japan's tragic tsunami created short-term demand dislocations, spreads in Italian and Spanish debt started to widen, high oil prices started to negatively affect consumer confidence, and Purchasing Manager's data started to rapidly decline from the low 60s to the low 50s. Ten-year bond yields fell materially from 3.74% to 3.16% by the end of the second quarter in response to these slowdown signs.

During the third quarter, the global growth/inflation thesis was debunked. Equities declined globally and Italian and Spanish ten-year bond yields skyrocketed, putting even more downward pressure on

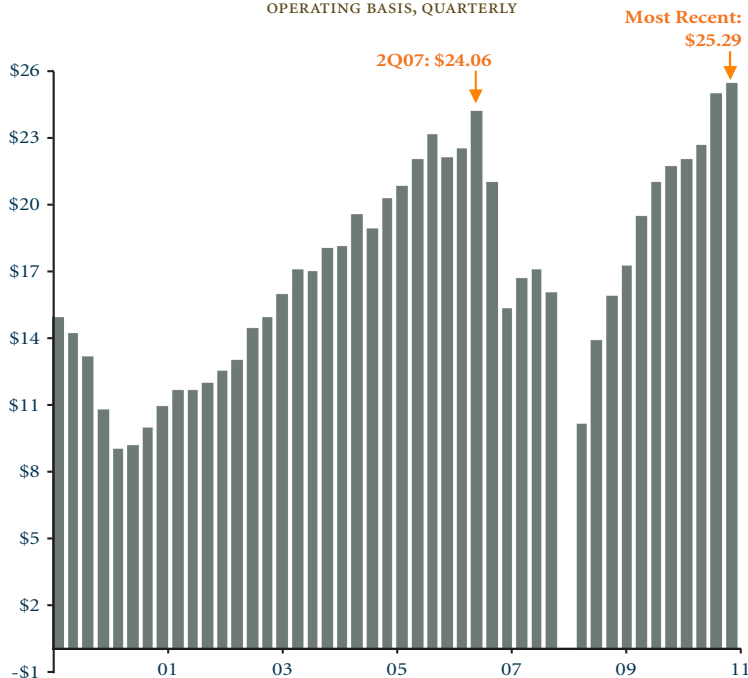
European banks' balance sheets. Investors began to discount a full blown European recession not just as a possibility but as a virtual certainty. Risks of a "Lehman-type moment" increased significantly along with global contagion fears. In the U.S., the inability of both political parties to make any material progress on our own deficit issues did little to improve waning investor confidence.

After double-digit declines for equities in the third quarter, equities rebounded sharply in the fourth quarter as fears of an imminent global recession receded. Economic data points in the fourth quarter continued to hold up and even slightly improve overall. Even Europe did not have a meaningful negative impact on U.S. corporate profits (but U.S. companies are planning and forecasting weakness in Europe next year). We are by no means confident that policymakers have permanently resolved the European Sovereign Debt Crisis, but the risks seem fairly well known at this point. European banks are clearly undercapitalized and will need to raise more capital in the marketplace, sell assets and shrink balance sheets, or be nationalized in the future. Fiscal discipline and unity in the European Union (EU) seem to be improving, which is a prerequisite for any substantive longer term solution for the EU. The strong rebound in the fourth quarter virtually eliminated prior losses, and the S&P 500 ended slightly positive for the year.

In spite of the dominant influence this year of the European Sovereign Debt Crisis on global financial market prices, domestic businesses continued to perform admirably throughout the year. In fact, S&P 500 companies reported all-time highs for profits in the third quarter (\$25.29 per share), exceeding the prior peak of \$24.06 set in the second quarter of 2007 (See chart: *S&P 500® Earnings Per Share*).

S&P 500® EARNINGS PER SHARE

OPERATING BASIS, QUARTERLY



Source: Standard & Poor's, J.P. Morgan Asset Management

EPS levels are based on operating earnings per share. Most recently available is a 3Q11 99% complete estimate.

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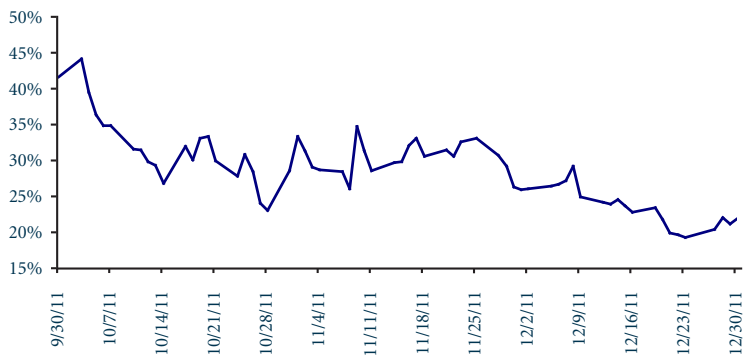
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Cash has continued to pile up on corporate balance sheets and is now exceeding 28% of current assets, another all-time high. Corporate America is in outstanding shape with inventory and headcount levels in very reasonable condition. With all of the crosscurrents evident in the macroeconomic global picture, so far the microeconomic picture in this country continues to be a bright spot.

OUTLOOK

We believe the economy will continue to grow at a below average rate over the next year or two. It will take time to work off excessive government debt in the U.S. and abroad. This sub-par recovery by historical standards seems likely to persist as developed countries around the globe deal with fiscal austerity programs. This process will slow, but not eliminate, global growth and we do not believe a recession triggered by European Sovereign Debt issues is inevitable next year or even highly likely. S&P 500 earnings should continue to grow, albeit at a more modest pace than over the last three years. It is difficult to imagine how U. S. Treasury prices can continue to dramatically outperform other asset classes from current interest rate levels, but many credit-spread based bonds (high yield, emerging market debt) appear moderately attractive. The VIX (Market Volatility Index) has dramatically declined from the low 40s to the low 20s over the last three months, indicating less investor fear as equity prices have recovered sharply (See chart: *Market Volatility Index*).

MARKET VOLATILITY INDEX

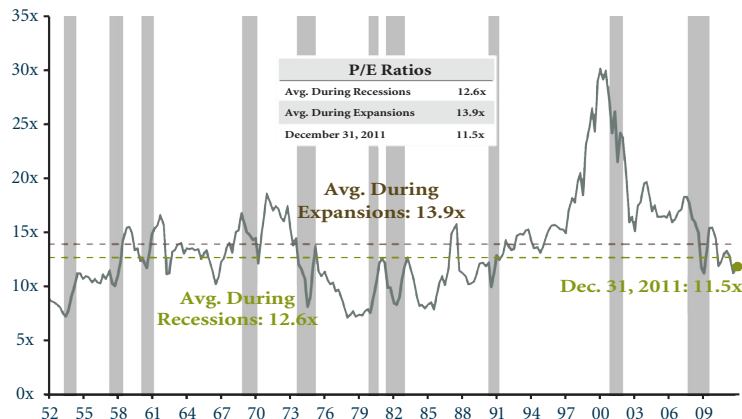


Source: Bloomberg

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Unfortunately, volatility will likely persist well into 2012 as investors continue to grapple with an uncertain macroeconomic environment. This tug of war between robust company fundamentals and weak macroeconomic trends (housing, excessive fiscal debt, and unemployment) seems likely to continue over the next year. Valuation support for the S&P 500 continues to be favorable as earnings have continued to grow while stock prices have gone sideways (See chart: *Lagged P/E Ratio – All U.S. Corporations*).

Lagged P/E Ratio – All U.S. Corporations



Source: BEA, Federal Reserve Board, Wilshire Associates, J.P. Morgan Asset Management
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At Kayne Anderson and Rudnick, our equity investment focus on specific company fundamentals and long-term investment horizon benefited our clients in 2011. Our investment returns were very strong relative to each strategy's respective benchmark. Conversely, many of our competitors found 2011 difficult to navigate and were easily whipsawed due to the tremendous volatility. As always, we will continue the search for alpha for our clients through our quality orientation and microeconomic analysis.

We appreciate your trust and confidence in these volatile markets and welcome any questions you may have.



DOUG FOREMAN, CFA
Director of Equities

Doug Foreman, CFA, is Director of Equities with primary responsibilities for evolving all aspects of the equity investment process and for overseeing product development. He has approximately 25 years of investment experience.

The S&P 500® Index is a market capitalization weighted index which includes 500 of the largest companies in leading industries of the U.S. economy. The MSCI® EAFE Index is a free float-adjusted market capitalization index that measures developed foreign market equity performance, excluding the U.S. and Canada. The MSCI® Emerging Markets (EM) Index is a free-float adjusted market capitalization index tracking the equity performance of global emerging markets. The Russell 2000® Index is a market capitalization-weighted index of the 2,000 smallest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. The Barclays Capital U.S. Aggregate Bond Index is a market value weighted index that tracks the daily price, coupon, pay downs, and total return performance of fixed-rate, publicly placed, dollar-denominated, and non-convertible investment grade debt issues with at least \$250 million par amount outstanding with at least one year to final maturity. Performance is calculated on a total return basis with dividends reinvested. The indexes are unmanaged and not available for direct investment.

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