Stephens
Investment Management Group®

STEPHENS MID CAP GROWTH SEPARATE ACCOUNT

QUARTERLY COMMENTARY

FIRST QUARTER 2017

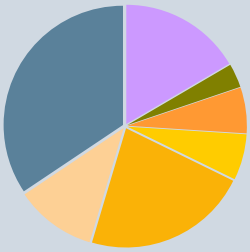
TOP 10 HOLDINGS[1]

COMPANY	% of PORTFOLIO
1. Cognex Corporation	2.11%
2. MercadoLibre, Inc.	2.05%
3. IDEXX Laboratories, Inc.	2.04%
4. SVB Financial Group	2.04%
5. Microchip Technology Incorporated	1.85%
6. Ulta Beauty Inc	1.76%
7. MarketAxess Holdings Inc.	1.73%
8. NVIDIA Corporation	1.72%
9. CoStar Group, Inc.	1.60%
10. Ross Stores, Inc.	1.57%

Excludes Money Market Fund Holdings. Portfolio holdings and asset allocations are subject to change and are not recommendations to buy or sell a security. Current and future portfolio holdings are subject to risk.

SECTOR WEIGHTINGS[1]

Consumer Discretionary	16.56%
Consumer Staples	3.24%
Energy	6.22%
Financials	6.24%
Health Care	22.35%
Industrials	10.99%
Information Technology	34.40%
Materials	0.00%



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MARKET OVERVIEW

The first quarter of 2017 was dominated by news relating to the new Trump administration. As reality set in, the post-election speculation and excitement about healthcare reform, tax reform, and fiscal stimulus began to fade. Despite the daily barrage of headlines, animal spirits remained high and equity markets posted strong gains. The S&P 500® rose 6.07%. Investors pushed markets into record territory. The Dow Jones Industrial® average broke 20,000 and then 21,000 soon after. The S&P 500® hit all-time highs as well.

Volatility remained surprisingly low, especially given so much macro-driven news.

While soft economic data still appears strong, the hard data has shown signs of slowing. Even though the Federal Reserve was able to raise rates in March without any market disruption, yields at the long end of the curve have begun to weaken. By the end of the quarter, the prospects of reflation have become less clear.

MID CAP GROWTH SEPARATE ACCOUNT COMPOSITE PERFORMANCE

Similar to last quarter, the strong returns of the broad market indices don't tell the whole story – it was the turbulence across economic sectors that drove relative performance. In fact, the winning and losing sectors were essentially reversed from the prior quarter. And the massive sector differences between the growth and value versions of Russell's indices were the primary drivers of their relative performance. The net result is that growth strategies bested value, and large cap beat small.

The Russell Mid Cap Growth® Index rose 6.89%. The Stephens Mid Cap Growth Strategy gained 9.74% (9.59% net) for the quarter.

Consumer Discretionary stocks lagged the broad market. There wasn't much positive data in the entire sector. Even though we are substantially underweight the sector, we continued to reduce exposure. We sold our stake in Buffalo Wild Wings, Inc. and Under Armour, Inc. – both had disappointing quarters. We trimmed our position in National CineMedia, Inc. as well.

Energy stocks gave up some of the returns they enjoyed from the prior quarter. Our stocks outperformed those in the benchmark, but were still in negative territory. Our overweight position hurt the strategy's performance. Crude prices sold off in March over concerns of an inventory build. Activity levels in North America continue to improve and we continue to believe the supply/demand imbalance has been remedied.

After an impressive Q4, Financials lagged the market this period. However, our holdings fared much better. While our bank holdings were essentially flat, our investment in MarketAxess Holdings Inc. drove our positive returns. They posted a stellar earnings result early in the quarter and the stock held onto those gains.

Industrials lagged the market (another reversal from Q4), and our portfolio was roughly in line with the benchmark. It was a fairly quiet quarter for Industrials.

Healthcare benefitted from the sector reversals – it was the best performer of the bunch. Our holdings related to pet health did very well. VCA Inc., a company focused on veterinary care and animal hospitals, was acquired for a significant premium. And IDEXX Laboratories, Inc. was one of our top contributors. Interestingly, all but two of our Healthcare stocks posted positive returns for the quarter.

Technology stocks rebounded from Q4 as well. Our overweight position here helped returns. MercadoLibre, Inc. was our single biggest contributor to returns. The company posted nearly perfect Q4 results. After the report, we trimmed some of our position just as a risk control measure. Mobileye N.V., a provider of technology which enables autonomous driving was acquired by Intel Corp. We had owned the stock since its IPO. Additionally, our software holdings generally did well, and this is where we have the most exposure.

PORTFOLIO CHARACTERISTICS[1]

Turnover was about as usual. We eliminated six positions and initiated four new ones. The strong performance in Technology combined with some new holdings resulted in a slight uptick in exposure. It is still our largest sector and now represents about 34% of assets. Healthcare ticked up to 22% and Consumer Discretionary rounded out the top three at just over 16%, down significantly from the prior quarter. Relative to the benchmark, we are still overweight Technology, Healthcare, and Energy, and underweight Real Estate, Materials, and Consumer.

Valuations expanded across the board. The weighted harmonic average P/E ratio on next twelve months earnings is over 25. For the Russell Mid Cap® Growth, the same measure is 20.3. Growth expectations didn't change too much. Our median holding is expected to grow earnings at 13.5% and revenues at 9.1%. Actual growth for the most recently reported quarter came in at very similar levels, 14.9% and 11.4% respectively. The metrics for the benchmark pale in comparison, at 11.0% (earnings) and 6.0% (revenues).

Our split between *core growth* and *earnings catalyst* companies was essentially unchanged. The mix is now 41% catalyst, 59% core.

[1]The information is shown as supplemental only and complements the full disclosure presentation located on the back. The Russell Midcap® Growth Index measures the performance of those Russell Midcap® companies with higher price-to-book ratios and higher forecasted growth values. You cannot invest directly in an index. The S&P 500® Index is a broad-based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general. The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index, which represents approximately 8% of the total market capitalization of the Russell 3000® Index. You cannot invest directly in an index.

OUTLOOK

Last quarter, our *Outlook* focused on the impact of ETF use in Q4. Digging into the matter, we realized how important the issue really is. We have just recently published a paper on the impact of the growth in ETFs and passive investing. If you haven't seen it yet, please check our website or call or email us.

As a result of having spent a great deal of time thinking about the implications of this ETF/Passive phenomenon, I have an interesting conclusion as it relates to our outlook: I am less certain about any near term market outlook, but more certain about the longer term. To explain that, I'll have to give you a bit of background…

Prior to the 1990s, most individual investors had their money with a stock broker. And that broker would help their clients invest in a handful of stocks. The '90s brought us the tremendous growth in mutual funds. Brokers began to outsource the stock picking to mutual fund managers. For a small fee they got the benefits of diversification, the expertise of a professional investment team, and the ability to gain exposure to more parts of the market. Just as the accumulation of assets by mutual fund managers was an enormous change in the market, the advent of ETFs has brought about another shift.

Since 2007 or so, the average wealth manager has been firing her mutual fund manager and allocating more assets to ETFs. Academia makes a powerful argument for passive investing, and the industry has embraced it. Before ETFs, the assets of an average investor were being allocated by a wealth manager, generally with a long term focus, and the managers of those allocations were making security selection decisions. Today the wealth manager is allocating their client assets among ETFs, and they have the ability to gain exposure to almost any market segment, industry, country, commodity, or factor - long or short - with a simple equity trade. The average wealth manager has become a master of the universe. But there's a dirty little secret with all of those assets: *no one is paying attention to security selection.*

Security selection is as much art as it is science, and every portfolio manager has a different approach, but the common function they all serve is determining whether or not the security in question is or will be worth more or less than its current price.

So when money goes into an ETF it is price (valuation) indifferent. It is simply seeking exposure. We've talked about this in prior commentaries, but it's worth mentioning again. We've previously pointed out some examples of this with USMV and IBB.

Actively managed assets represent only about 56% of the market, down from 80% just 11 years ago. The direction is clear. Already we are noticing signs of a structural change in the market. The price discovery process is not as robust as it once was. What will the market be like with active assets representing less than 50% of the market? Less than 40%? **What will be the catalyst to reverse this trend?**

Here's the other dirty secret*: even though investors are using ETFs and so-called passive vehicles, they are actively trading, maneuvering and rebalancing exposures across the market. This is not passive investing.* All you have to do is look at the daily volume in ETFs, and you'll understand just how active this market is.

With that background in place, maybe you can see where I'm heading. In the short run, the outlook is more uncertain than normal. There are a lot of investors wrestling the direct control of assets back, but at the same time ignoring company fundamentals. As more investors paint with a broad brush and are drawn to the flavor of the month, the performance disparity across sectors and factors will only expand.

The longer term is easier to see, in my opinion. There will be a reckoning day. It always comes. Sure, it's different this time. It's different every time. But human nature is what it is, and history repeats itself. The trend will extend for much longer than it should, and it will reach some extreme. There will be unintended consequences and collateral damage. People will be reminded why they used to hire active managers. Having a team of thoughtful professionals that painstakingly handpick individual securities based on the merits of that company will once again be in vogue. Until that day, we will be here doing what we've always done, picking those companies, but evolving and learning new tricks to deal with these changing times.

Earnings growth for a portfolio holding does not guarantee a corresponding increase in the market value of the holding or the portfolio. Earnings Growth is a measure of growth in a company's net income over a specific period, often one year. **Return on Equity** is the amount of net income returned as a percentage of shareholders equity and measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested.

IMPORTANT LEGAL DISCLOSURES

Year	Total Firm Assets (millions)	Strategy Assets*		Composite Assets		Annual Performance Results				3 Yr Annualized Standard Deviation	
		USD (millions)	Number of Accounts	USD (millions)	Number of Accounts	Composite		Russell Midcap® Growth	Composite Dispersion	Composite Gross	Russell Midcap® Growth
						Gross	Net				
2016	3,658	287	13	201	9	7.98%	7.24%	7.33%	0.09%	13.13%	12.17%
2015	2,903	152	12	38	10	-0.27%	-1.01%	-0.20%	N.A.	12.01%	11.29%
2014	3,436	165	6	31	4	4.19%	3.40%	11.90%	N.A.	11.71%	10.87%
2013	3,076	155	6	35	4	34.63%	33.60%	35.74%	N.A.	13.54%	14.62%
2012	1,222	85	6	7	2	16.74%	15.78%	15.81%	N.A.	16.44%	17.91%
2011	933	40	3	1	1	3.26%	2.44%	-1.65%	N.A.	18.13%	20.82%
2010	919	25	2	1	1	30.65%	29.63%	26.38%	N.A.	24.46%	26.37%
2009	554	16	2	1	1	42.29%	41.18%	46.29%	N.A.	22.61%	24.01%
2008	387	12	2	1	1	-44.27%	-44.69%	-44.32%	N.A.	N.A.	N.A.
2007	391	19	2	1	1	25.53%	24.73%	11.43%	N.A.	N.A.	N.A.

*Strategy Assets are shown as supplemental information as these assets include mutual fund and UMA assets which are managed within the Mid Cap Growth Strategy
N.A. - Composite Dispersion information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. Information for the 3-Yr Annualized Standard Deviation is not presented because there is less than 36 months of performance data.

The investment objectives, risks, charges and expenses should be carefully considered before investing. SIMG nor their representatives provide legal or tax advice. Please consult your tax advisor before making any decisions.

There are additional risks associated with investments in smaller and/or newer companies because their shares tend to be less liquid than securities of larger companies. Further, shares of small and new companies are generally more sensitive to purchase and sales transactions involving the company's stock and to changes in the company's financial condition or prospects, and, therefore, the prices of such stocks may be more volatile than those of larger company stocks. Clients' investment results and principal value will fluctuate.

Mid Cap Growth Separate Account Composite *contains fully discretionary accounts invested primarily in mid cap common stock of U.S. companies. Under normal conditions, securities purchased for this composite have market capitalizations between $1 billion and the market capitalization of the largest company in the Russell Midcap® Growth Index at the time of initial purchase, which appear to have clear indicators of future earnings growth or that appear to demonstrate other potential for growth of capital. In addition to common stock the composite may also purchase convertible and preferred stock as well as certain Exchange Traded Funds. This composite is actively managed and securities in the composite are frequently purchased and sold by the manager. For comparison purposes the composite is measured against the Russell Midcap® Growth Index.*

Stephens Investment Management Group, LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Stephens Investment Management Group has been independently verified for the periods December 1, 2005 through December 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 Mid Cap Growth Separate Account Composite has been examined for the periods June 2, 2006 through December 31, 2016. The verification and performance examination reports are available upon request.

Stephens Investment Management Group, LLC is a registered investment advisor specializing in equity investment management, specifically small and mid-capitalization growth companies. The firm maintains a complete list and description of composites, which is available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results.

The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of fees and include the reinvestment of all income. Net of fee performance is calculated using actual fees incurred. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. The management fee schedule begins at 1.00% of assets under management. Actual investment advisory fees incurred by clients may vary. The Mid Cap Growth Separate Account Composite was created June 2, 2006.

Prior to September 1, 2011, composite policy required the temporary removal of any account from the composite which incurred a client initiated significant cash inflow or outflow of 10% or more of the value of the net assets of the account in any 30 day period. The temporary removal of such an account occurred at the beginning of the month in which the significant cash flow occurred and the account re-entered the composite at the beginning of the month after the cash flow. This policy was deleted effective September 1, 2011. Additional information regarding the treatment of significant cash flows is available upon request.

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The annual composite dispersion is an asset-weighted standard deviation calculated for the accounts in the composite the entire year.