Great-West Profile Funds

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Off the charts

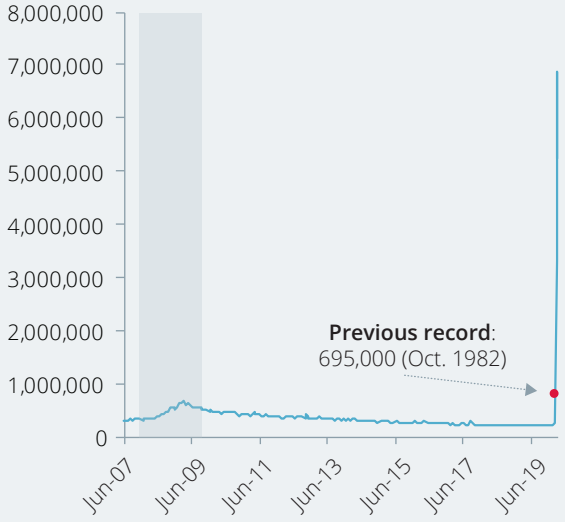
Last quarter we used this space to describe a robust, 9%-plus advance in the S&P 500® Index that even then looked a little suspicious to us given advancing equity market valuations, an obvious flattening of corporate earnings and emerging signs of softness in some of the very things that had underwritten the decade-long expansion of the U.S. economy — things like consumer confidence, industrial production and the previously unassailable strength of the U.S. labor market. This nascent slowdown was accompanied by a steady drumbeat of geopolitical risks that, at the time, seemed significant: a flare-up of U.S.-Iranian military tensions and the not-quite-resolved U.S.-China trade war chief among them.

In retrospect, those risks seem almost quaint given the massive damage currently being wrought by the COVID-19 pandemic. The human toll has of course been awful: by mid-April, 130,000 people had succumbed to the disease, with 2 million cases touching populations in virtually every corner of the globe. While there are signs that infection growth rates have slowed, no one can yet predict when this horror will end.

Likewise, no one can know for sure how deep or how prolonged the global recession that COVID-19 has spawned will be. Efforts to slow the advance of the virus, while prudent and necessary from a medical standpoint, have effectively hung a "Closed for Business" sign on the worldwide economy — something that has never happened, not even during the two world wars of the last century. But however unpredictable the economic environment has become, one thing is certain — the damage to the global economy has been significant, and the reverberations will continue long after the advance of the virus has slowed.

Off the charts, part 1

More jobless claims were filed than at any point in history



Evidence that the COVID-inspired recession is truly exceptional isn't hard to come by, but the spike in joblessness is truly sobering: During the four weeks since stay-at-home orders were first issued, more than 22 million U.S. workers filed for first-time unemployment benefits. That's more than eight times the previous record for a four-week span, which was set way back in October 1982.

The speed with which these workers are put back to work will largely determine the speed and shape of the post-COVID recovery.

Source: U.S. Department of Labor, FRED St. Louis Federal Reserve.

Hints about how severe the damage of near-universal orders to stay at home and shelter in place can be found in any number of economic indicators, ranging from retail sales to consumer confidence to various surveys of industrial output — many of which have surged to highs (or lows) not seen in a generation.

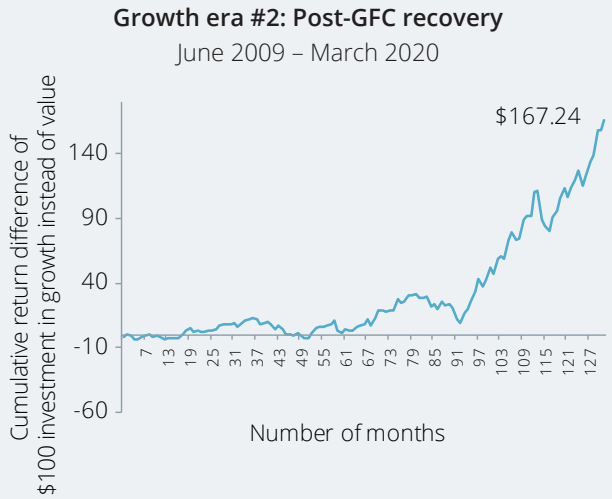
The most striking example by far, though, is the enormous spike in the number of Americans filing for unemployment benefits: More than 21 million workers applied for benefits during the four weeks since the first and most visible stay-at-home orders went into place, obliterating previous records for jobless claims by nearly a factor of 10 (and making time-series charts of historical data for this series all but unreadable). The speed with which these employees are put back to work when the crisis finally fades will in large part determine how deep and long-lasting the COVID-19 recession ultimately proves to be.

Capital markets had a few off-the-charts moments of their own during the quarter. So-called "risk assets" (equities and high-yield bonds, for example) sold off across the board while safe havens (like government bonds) held up quite well. In some cases, the selling followed a predictable pattern — those areas of the market deemed most likely to suffer the most amid the economic chaos sold off hardest. For example, mid- and small-cap stocks significantly underperformed larger-cap stocks out of fear that smaller firms are generally more exposed to the business cycle and would have a harder time weathering a near-total shutdown in demand — especially a shutdown of indeterminable length.

But other results were somewhat more surprising to us. Take, for example, the relative outperformance of growth equities during the first quarter, when U.S. growth stocks declined significantly less than their

Off the charts, part 2

The dispersion between growth and value stocks has grown to historic proportions



Everyone is familiar with the historic run that growth had versus value during the "dot.com" era of the late 1990s and early 2000s. But growth's current dominance has now surpassed that era in terms of both duration and magnitude. At its peak, the dot.com growth era lasted 68 months and netted growth investors an advantage of $154 over value before reversion to the mean took over.* But since the end of the Great Recession in June 2009, growth's outperformance over value has reached $167 over 129 months (and still counting). That makes us wonder when (and how powerful) the reckoning will be when it finally comes.

Source: Morningstar, GWI calculations. Represents the difference between investing $100 in the Russell 1000 Growth Index minus $100 in the Russell 1000 Value Index for the periods indicated.

value-oriented peers across all capitalization ranges. That's perhaps even more surprising when you consider the starting point for each investment style. Although valuations were rich across the board at the start of the year, growth stocks were trading at earnings multiples far in excess of their longer-term averages, while value stocks were within spitting distance of theirs.

The first quarter's dramatic sell-off had the predictable effect of compressing these valuations, leaving growth stocks much closer to historical norms in the process. But as mentioned above, value stocks fell even harder than their growthier peers, leaving price-to-earnings multiples of that segment of the market well below where they typically trade. The result? The cheapest sectors of the market got even cheaper, at least on a relative basis.

Performance of the Great-West Profile Funds

This discussion matters to our shareholders because, although we carefully maintain significant exposure to both growth- and value-oriented investments, our portfolios typically carry slightly more exposure to value than to growth. That, together with our tendency to invest more heavily in smaller- and mid-sized companies (and to carry slightly more exposure to non-U.S. stocks than our average competitor), worked against performance during the first quarter of 2020 and was enough to cause each fund in the Profile series to underperform its benchmark. Peer-relative performance was somewhat more mixed and, as with prior periods, was influenced by the relatively wide range of strategic equity allocations evident in each funds' respective Morningstar peer group. Specific to the first quarter of 2020, the first four funds in the Great-West Profile series (conservative, moderately conservative, moderate and moderately aggressive funds) each fell toward the middle of their respective peer groups, while the aggressive Profile fund lagged its competitors significantly — a function of its 100% allocation to stocks during a period in which equity markets declined sharply.

We've discussed these same dynamics in prior versions of this commentary. In fact, our small but strategically important bias toward value has also been a consistent headwind to performance for several quarters — if not years — running, and while it can be difficult to maintain this conviction in the face of such persistent difficulties, we continue to believe that our positioning along the growth-versus-value spectrum is appropriate for our investors. This is particularly true because the historic run in growth stocks now rivals that which was in place during the infamous "tech bubble" at the beginning of this century and has created distortions that seem unsustainable to us, such as the high degree of concentration that has emerged in large-cap growth indices like the Russell 1000 Growth Index, where the five largest names — all of which are technology stocks — account for more than a quarter of the index. By contrast, the five largest stocks in the Russell 1000 Value Index account for only 8% of the index and represent at least three distinct industries (financials, consumer staples and technology).[1]

However attractive the fundamentals of technology and other fast-growing businesses are, we believe that a properly diversified portfolio must fully reflect the entire range of economic activity in our wonderfully diverse and infinitely flexible worldwide economy. Perhaps more to the point, we believe that the historic run of outperformance enjoyed by growth will eventually end, and we will again be rewarded as relative valuations realign with historical norms.

Likewise for our tendency to slightly overweight small- and mid-capitalization stocks compared to our peers. This bias also worked against us as worries related to the COVID-19 pandemic caused investors to focus on those asset classes perceived to be less exposed to the economic damage currently being wrought by the virus. As described above, smaller companies are often thought to carry more exposure to extreme ups and downs of the business cycle, which caused them to decline more than their larger peers during the first quarter of 2020. While we generally agree with this interpretation, we again believe that proper

1 FTSE Russell, March 31, 2020, and Morningstar.

diversification requires that we maintain a disciplined exposure to all areas of the market, not merely those that seem to temporarily present the most favorable characteristics at any given point in time. For now, that includes small- and mid-cap stocks. Furthermore, we are encouraged by the fact that the various stimulus programs put in place by U.S. officials in the wake of the COVID crisis have contemplated and attempted to address the unique risks faced by smaller enterprises, and we look forward to a robust recovery when the economy returns to a more normal footing.

In terms of what has worked well for the funds, we are encouraged that the vast majority of our underlying investment managers performed up to (or exceeded) our expectations during what proved to be an extremely volatile quarter. As we have stated in the past, we view our ability to research, hire and retain world-class investment talent as a core competence and our most crucial advantage over other strategies, and our manager selection results once again bore that out.

Outlook

Make no mistake, these are exceptional times. There is no template or playbook for the challenges we face as a society, and we, like everyone else, are unable to offer any special insight as to when things will return to normal. Rest assured, though, that our nation will persist, and capital markets will eventually return to a time when things like drone strikes, commodity price wars and tit-for-tat trade sanctions are once again enough to move the needle. Until then, we will continue to create the broadest, most diversified portfolios we know how to create, enlisting world-class managers to invest with along the way. In closing, thank you for your continued confidence and investment. Please stay healthy and safe.

Morningstar ratings and rankings as of March 31, 2020

Rating based on risk-adjusted returns and ranking based on total return

FUND NAME	TICKER	INCEPTION	CATEGORY	RATING/ TOTAL # OF FUNDS OVERALL	3-YEAR	5-YEAR	RANK[1]/ # OF FUNDS 1-YEAR
Great-West Aggressive Profile Instl	MXGTX	5/1/15	U.S. Fund Allocation - 85%+ Equity	★★★ 176	★★★ 162	★★★ 144	145/176
Great-West Moderately Agg Profile Instl	MXHRX	5/1/15	U.S. Fund Allocation - 70-85% Equity	★★★ 332	★★★ 307	★★★ 276	173/332
Great-West Moderate Profile Instl	MXITX	5/1/15	U.S. Fund Allocation 50-75% Equity	★★★ 687	★★★ 640	★★★ 561	495/687
Great-West Moderately Cnsrv Profile Instl	MXJUX	5/1/15	U.S. Fund Allocation 30-50% Equity	★★★ 561	★★★ 516	★★★ 428	319/561
Great-West Conservative Profile Instl	MXKVX	5/1/15	U.S. Fund Allocation 15-30% Equity	★★★ 198	★★★ 180	★★★ 155	129/198

Fund performance as of March 31, 2020

FUND NAME	TICKER	INCEPTION	NET EXPENSE RATIO[2] (%)	GROSS EXPENSE RATIO[2] (%)	1-YEAR RETURN (%)	3-YEAR RETURN (%)	5-YEAR RETURN (%)	SINCE-INCEPTION RETURN (%)
Great-West Aggressive Profile Instl	MXGTX	5/1/15	0.10	0.10	-16.13	-0.83	2.05	2.01
Great-West Moderately Agg Prfl Instl	MXHRX	5/1/15	0.07	0.10	-10.69	0.36	2.32	2.31
Great-West Moderate Profile Instl	MXITX	5/1/15	0.04	0.10	-8.04	0.89	2.41	2.40
Great-West Moderately Cnsrv Pfl Instl	MXJUX	5/1/15	0.02	0.10	-5.53	1.23	2.36	2.36
Great-West Conservative Profile Instl	MXKVX	5/1/15	0.02	0.10	-3.23	1.49	2.28	2.27

1 A lower percentile ranking is more favorable (higher relative returns).

2 Gross expense ratios are the funds' total annual operating costs expressed as a percentage of the funds' average net assets over a given time period. They are gross of any fee waivers or expense reimbursements. Net expense ratios are the expense ratios after the application of any voluntary or contractual waivers or reimbursements and are the actual ratios that investors paid during the funds' most recent fiscal year. Expense ratios are subject to change. All contractual fee waivers for the Great-West Profile Funds expire on April 30, 2020. Absent waivers or reimbursements, the performance would have been lower.

Performance for institutional class shares before their inception is derived from the historical performance of initial class shares, which has not been adjusted for the lower expenses; had it, returns would have been higher.

Current performance may be lower or higher than performance data shown. Performance data quoted represents past performance and is not a guarantee or prediction of future results. For performance data current to the most recent month end, please visit greatwestfunds.com. The investment return and principal value of an investment will fluctuate so that, when redeemed, shares/units may be worth more or less than their original cost.

Please consider the investment objectives, risks, fees and expenses carefully before investing. For this and other important information, you may obtain mutual fund prospectuses from your registered representative or by visiting greatwestfunds.com. Read them carefully before investing.

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Morningstar Percentile Rankings are based on the average annual total returns of the funds in the category for the periods stated and do not include any sales charges or redemption fees, but do include 12b-1 fees and the reinvestment of dividends and capital gains distributions. The highest (or most favorable) percentile rank is 1 and the lowest (or least favorable) percentile rank is 100. Rankings for share classes without a 3-, 5- or 10-year history, as applicable, is based on extended performance. Different share classes may have different rankings.

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Asset allocation and diversification do not ensure a profit and do not protect against loss in declining markets.

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