Eagle Insight

EAGLE Asset Management
AN AFFILIATE OF CARILLON TOWER ADVISERS

Large Cap Core

Third Quarter | 2018

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The risks associated with Large Cap Core investing are based on the expectation of positive price performance due to continued earnings growth or anticipated changes in the market or within the company itself. However, if a company fails to meet that expectation or anticipated changes do not occur, its stock price may decline. Moreover, as with all equity investing, there is the risk that an unexpected change in the market or within the company itself may have an adverse effect on its stock. Investing in growth-oriented stocks involves potentially higher volatility and risk than investing in income-generating stocks. The biggest risk of equity investing is that returns can fluctuate and investors can lose money.

Market Overview

United States equity markets were generally positive in the third quarter of 2018; however, globally, returns were mixed.

After eight years of modest growth in the United States, some investors may be concerned about the late-stage economic cycle, especially as valuations become increasingly stretched. Further, President Trump's actions compound some investor worries. In the most recent trade war escalation with China, the U.S.-imposed tariffs on another $200 billion in goods. This is another big step toward a broader conflict that may become difficult to reverse and could weigh greatly on the global economy.

However, much of the recent data for the U.S. economy remains bullish, as economic growth and earnings still appear strong. In addition, many surveys of U.S. investors continue to suggest plenty of optimism. The U.S. aside, much of the rest of the world remains in the early stages of recovery. Overall, the International Monetary Fund (IMF) expects global gross domestic product (GDP) to increase 3.9 percent in 2018 and 2019, from 3.6 percent in 2017, with each of the world's major economies firmly positive. However, the IMF warned that the expansion is becoming less even, as the rate of growth appears to have peaked in some major economies and higher oil prices and currency pressures have caused downward revisions to some emerging market projections. Chinese equities sold off significantly during the third quarter on concerns of a GDP slowdown or debt crisis. The Chinese government seemingly failed to settle nerves when reporting 6.7 percent economic growth in the second quarter, comfortably above their 6.5 percent GDP growth target for 2018 . According to a Reuters' poll, analysts expect the People's Bank of China (PBOC) to keep its benchmark lending rate unchanged at 4.35 percent through at least the end of 2019. The Federal Reserve (Fed) again raised the Fed funds rate by 0.25 percent in September to a target range of 2.00-2.25 percent. It represents the eighth rate hike since 2015, and now investors are looking for clues about next steps given low inflation and low growth. Federal Reserve Chair Jerome "Jay" Powell noted the economy is strong enough that low rates are no longer necessary – a shift the Fed marked by ending its description of its policy as "accommodative". Mr. Powell warned that a permanent shift to a "more protectionist world" would hurt the U.S. and global economies, but added that for now, he expects the overall economic impact to remain relatively modest.

The global benchmark for oil, Brent Crude, is up over 20 percent this year, closing September at $82, the highest level since 2014 . Prices are up partly because of the sanctions imposed on Iran, due to take effect in November but already leading to a decrease into that nation's oil output . In addition, the collapse in Venezuela's output, caused by political instability and infrastructure failure , certainly figures into the equation. Higher oil prices can act as a drag on global growth, with particular impact on the manufacturing and transportation sectors.

Portfolio Review[1,2]

During the third quarter of 2018, the Large Cap Core portfolio underperformed its S&P 500 Index benchmark. Stock selection detracted from performance; however, allocation was slightly positive. An overweight position in Energy detracted from performance while an underweight to Real Estate and Consumer Staples contributed to performance. Stock selection was weakest within Consumer Discretionary and Materials, but strong within Financials and Utilities.

At the start of the quarter, as compared to its S&P 500 benchmark, the Large Cap Core portfolio was most overweight the Information Technology and Financials sectors, and most underweight Consumer Staples and Real Estate. By the end of the quarter, the portfolio was most overweight the Information Technology and Health Care sectors, and remained most underweight Consumer Staples and Real Estate. Within the universe of S&P 500, Health Care and Industrials had the strongest returns, while Energy and Materials were weakest.

Apple designs, manufactures, and markets mobile communication devices, personal computers and media devices. The stock performed well after its fiscal third quarter earnings release included better-than-expected top and bottom line results. The company held its product launch event this quarter where the only big surprise was higher-than-expected prices for the new line-up of iPhones.

Microsoft develops and markets software and hardware services. The company delivered another stellar quarter driven by continued strength in corporate IT spending and solid execution across all three business segments. Microsoft also announced a quarterly dividend increase of about 9.5 percent.

Amazon.com, the world's largest online retailer, rose following its second quarter earnings release. The company posted strong earnings, led largely by Amazon Web Services (AWS) and advertising as well as improving fulfillment efficiency and stronger margin guidance.

JPMorgan Chase provides global financial services and retail banking. Shares outperformed peers on a down day for bank stocks as the company posted a strong beat across the board for Q2 earnings. JP Morgan also confirmed a quarterly dividend increase.

CVS Health Corporation, an American integrated pharmacy health care provider, announced solid performance in the quarter driven by better than expected Pharmacy Benefits Management (PBM) performance, cost controls, and lower taxes. The company reiterated it is on track to close its acquisition of Aetna by early fourth quarter.

Facebook, the social media company, missed estimates on revenue for the first time in three years. The stock hit a record high before earnings were released, but it tanked after hours. The company expects the revenue slowdown to continue. While Facebook still reported growth this quarter, it was not on par with past performance. In addition, operating margins were guided down.

Lear Corporation manufactures automobile parts including seating systems, wiring harnesses, body control electronics, wireless products and audio systems. The company's shares traded down following its first earnings miss in several years as a trucking strike in Brazil and softening sales in China impacted revenue and margins.

Electronic Arts, Inc. (EA) is a global interactive entertainment software company. First quarter revenue and EPS came in ahead of expectations; however, FIFA slowed in the quarter, driving live service growth to 7 percent, down from an average of ~30 percent growth in the prior four quarters. EA also announced a one-month delay for the release of Battlefield to deliver the best possible experience for gamers, but suspicion exists considering missteps around last year's release.

E*TRADE Financial Corp. engages in the provision of investment and online stock brokerage services. The company's stock price fell after JP Morgan Chase announced it will roll out a new

Top 10 Holdings

Microsoft Corporation
Apple
JPMorgan Chase
Amazon.com
UnitedHealth Group
Bank of America
Home Depot
Alphabet Class C
Alphabet Class A
Cisco Systems

The information provided above should not be construed as a recommendation to buy, sell or hold any particular security. The data is shown for informational purposes only and is not indicative of future portfolio characteristics or returns. Portfolio holdings are not stagnant and may change over time without prior notice. Past performance does not guarantee future results. Please note that the holdings identified do not represent all of the securities purchased, sold or recommended for the composite. They are provided for informational purposes only. Eagle, its affiliates or their respective employees may have a position in the securities listed. Please contact your financial advisor to obtain the calculation's methodology and/or a list showing every holding's contribution to the overall composite's performance during the measurement period.

Large Cap Core

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	Top Securities	Average Weight (%)	Security Contribution to Portfolio Return
Large Cap Core	Apple	4.80	0.99
	Microsoft	4.98	0.77
	Amazon	3.35	0.55
	JPMorgan Chase & Co.	3.81	0.34
	CVS Health Corporation	1.33	0.28

Bottom Securities	Average Weight (%)	Security Contribution to Portfolio Return
Facebook Class A	2.50	-0.42
Lear Corporation	1.37	-0.29
Electronic Arts	0.63	-0.18
E*TRADE Financial	0.77	-0.12
PulteGroup	0.86	-0.11

* as of Sept. 28. The information provided above should not be construed as a recommendation to buy, sell or hold any particular security. The data are shown for informational purposes only and are not indicative of future portfolio characteristics or returns. Portfolio holdings are not stagnant and may change over time without prior notice. Past performance does not guarantee future results. Please note that the holdings identified do not represent all of the securities purchased, sold or recommended for the composite. They are provided for informational purposes only. Eagle, its affiliates or their respective employees may have a position in the securities listed. Please contact your financial advisor to obtain the calculation's methodology and/or a list showing every holding's contribution to the overall composite's performance during the measurement period.

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PulteGroup, Inc. engages in the homebuilding business and is also involved in mortgage banking and title operations. An extended housing cycle, combined with climbing interest rates, put downward pressure on the group.

Outlook[1]

Domestic stocks have been able to climb a wall of worry, and remain near historic highs, despite the escalating trade wars. Outside the U.S., the potential for tighter monetary policy and the prospect for a reversal in the trend towards globalization rattled investors. While positive news on many of the macro fronts continues, as always, stocks face some hurdles in the short term.

Current estimates for S&P 500 year-over-year earnings growth stand at approximately +21% ; it could be difficult for the majority of companies to beat those elevated expectations. For now, earnings growth remains a key support for domestic stocks, and the healthy corporate picture is boosting the consumer via job growth and confidence.

With Congress slated to inject significant fiscal stimulus over the next two years, the Fed will aim to avoid economic overheating. This late-cycle tug of war between fiscal policy and monetary policy is unusual, and potentially dangerous. Futures markets now anticipate the Fed will raise rates once more this year, three times in 2019 and once in 2020. As rates rise, pressure will increase on the already frothy housing market, a key driver for the U.S. economy.

In the short term, the new tax cuts will benefit many Americans, and the spending bill should add to economic growth. In the long term, while worrisome, it is difficult to forecast the impact of larger deficits. Adding to the already complicated picture, the government has enacted substantial fiscal stimulus at a time when the economy is at essentially full employment.

The intensifying trade battles could potentially disrupt the world's economies, as U.S. businesses source roughly 40 percent of their revenues from overseas ; therefore, any disruption to global trade could be very damaging. Meanwhile, the ability of corporate management to be decisive in planning for the future may be compromised by the unsteady environment, impacting business confidence and capital expenditures.

Key elections in Mexico, Turkey, and Italy added volatility across global financial markets this year, amid a rising trend in populism. Looking forward, the run-up to Brazil's election on October 7 has been especially polarizing, including an assassination attempt on one of the candidates. In the U.S., the November 6 midterm elections will be closely watched as Democrats seek to gain seats (and possibly a majority) in both the House and Senate.

Investors have a variety of issues to fret over, including ongoing political turmoil, tariff announcements, numerous contentious elections, etc. Sticking with a long-term investment approach is certainly more difficult to do when markets aren't going straight up; however, sell-offs and volatility indicate a healthier investing environment, which could help extend the current growth cycle. Our outlook for the remainder of 2018, and into 2019, remains guardedly optimistic. That said, we would be wise to expect more bumps in the road along the way.

1. References to specific securities are intended to illustrate the types of securities Eagle may hold in this portfolio. They are not intended as representations of specific investment recommendations that would have been profitable to an investor. Past performance is not a guarantee of future results. Opinions and estimates offered constitute Eagle's judgment and are subject to change without notice as are statements of financial-market trends, which are based on current market conditions. Investing involves risk, including the possible loss of principle.

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2. Source: FactSet.

[i] Source: Reuters
[ii] Source: Bloomberg
[iii] Source: Reuters
[iv] Source: Bloomberg
[v] Source: FactSet
[vi] Source: Bloomberg