

## Value

Second Quarter | 2019

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\*as of July 1.

Value investing is based on the potential for a company's stock price to rise based upon anticipated changes in the market or within the company itself. Value stocks have historically been sensitive to economic cycles and investor sentiment that can affect volatility and risk.

### Market Overview<sup>1</sup>

Despite an escalation in the U.S.-China trade conflict and a slowing global economy the US equity market, as measured by the Russell 1000® Value Index, appreciated 3.8% during the second quarter. We believe the main catalyst was a perceived shift in the Federal Reserve's outlook regarding interest rates, signaling that no more rate hikes are expected this year, or perhaps even a rate cut if economic conditions deteriorate. This reduced the concern for a major policy mistake and raised the appetite for equities. Cyclical sectors performed best during the quarter, including financials, technology and materials. Defensive sectors, including healthcare, utilities and REITs posted positive returns but lagged most sectors.

### Portfolio Review<sup>1,2,3</sup>

The Value portfolios outperformed the Russell 1000 Value Index benchmark on a gross and net basis during the second quarter. Strong stock selection within industrials, real estate and financials led performance. Stock selection in energy, consumer discretionary and a small cash position hurt performance.

Total System Services stock appreciated after the company entered into a merger agreement with Global Payments. The deal reflected an approximately 20% premium to the recent comparable closing price. We decided to sell the holding after the announcement to avoid any potential regulatory uncertainty.

Microsoft reported another impressive quarter, with most businesses performing well. Management also provided a high-level outlook for next fiscal year, with expectations for solid double-digit growth in revenues. Microsoft continues to win in the cloud business and grow margins as it achieves scale.

Prologis delivered solid performance in the second quarter, largely resulting from lower interest rates, which are generally beneficial to REITs.

Lockheed Martin appreciated following a strong quarter. Management announced revenue and earnings well ahead of consensus and increased guidance for the remainder of the year. The company continues to benefit from the trend of government outlays catching up to budgeting authorizations.

Honeywell reported financial results with revenue and earnings per share nicely ahead of consensus. This is in contrast to most industrial companies that are struggling to hit expectations due to weak U.S. industrial macro data. The company was still able to produce an acceleration in organic growth despite these issues.

Occidental Petroleum traded lower as the company embraced a bidding war with a much larger entity over a pure-play Permian exploration and production (E&P) company. The offer price was much larger than investors expected, leading to questions regarding the proposed synergy target.

Halliburton announced stronger earnings per share and revenues; however, shares traded lower due to weakness in pricing. Large E&P companies have been cutting spending and as a result, many energy service providers have been squeezed. Positively, management believes the worst in the pricing deterioration is now behind them.

Zimmer Biomet's underperformance can be attributed to a drawdown in investor sentiment after enthusiasm for the company's new robotic knee surgery platform peaked in mid-March. Concerns around the announced retirement of Zimmer's long time CFO also contributed to the stock's slide in late June,

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but his successor is viewed as a strong, experienced replacement.

Kroger shares traded lower after the company reported same-store sales below expectations. The company has struggled to increase sales following remodels in 2018. Management was able to improve margins, but lower fuel prices affecting Kroger's gas stations played a significant role.

ConocoPhillips stock fell following a strong run throughout the past year. The company delivered better than expected results, while continuing to focus on responsible capital spending. Production remains on track with previous guidance.

## Outlook

We just entered the longest U.S. economic expansion on record. July will mark the 121st month of growth since June 2009, when the last trough ended, as determined by the National Bureau of Economic Research (NBER). The previous record was 120 months of economic growth from March 1991 to March 2001.

Does that mean we should be concerned that the expansion is about to end? We do not believe so. Economic expansions don't just die of old age; something has to happen to end it. Usually this would either be an external shock to the economy, or an asset bubble popping, or because the Federal Reserve may cause a slowdown or a recession by raising rates too much. We don't see any asset bubbles currently, and it looks like the Fed is on hold with rate hikes for now, so we believe this economic expansion still has legs.

More worrisome for investors in the near-term might be the recent slowing in manufacturing activity, which has been a weak spot for the U.S. and global economies as escalating trade concerns and tariffs have put downward pressure on the sector. Consequently, corporate earnings are

expected to decline slightly versus last year in the second and third quarters of 2019. Fortunately, employment data has so far been unaffected and remained solid, but we will continue to monitor it closely. We expect earnings growth to gradually improve by year-end, which should be good news for equities in general.

We feel very confident about the way we have positioned our strategy for the current economic backdrop.

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## Top 10 Holdings

Microsoft  
Honeywell International  
Prologis  
JPMorgan Chase  
PNC  
Merck  
Cisco  
AT&T  
Zimmer Biomet  
Laboratory Corporation of America

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.

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	<b>Top Securities</b>	<b>Average Weight (%)</b>	<b>Security Contribution to Portfolio Return</b>	<b>Bottom Securities</b>	<b>Average Weight (%)</b>	<b>Security Contribution to Portfolio Return</b>
<b>Value</b>	Total System Services	1.95	0.68	Occidental Petroleum	1.46	-0.41
	Microsoft	4.54	0.60	Halliburton	1.06	-0.27
	Prologis	4.24	0.50	Zimmer Biomet	2.79	-0.23
	Lockheed Martin	2.42	0.49	Kroger	1.56	-0.18
	Honeywell	4.42	0.45	ConocoPhillips	1.83	-0.17

\* as of June 28, 2019. 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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3. Source: FactSet.

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