

# Portfolio Commentary

## Mid-Cap Value Equity

Q3 | 2018

### MARKET REVIEW

Strong fundamentals and positive earnings momentum helped to lift stock markets higher during the quarter, with large caps generally outperforming small caps and growth leading value. The Russell Midcap® Value Index rose 3.30% led by impressive gains in the telecommunication services (+16.68%), industrials (+9.60%), healthcare (+9.23%), and information technology (+7.60%) sectors, while the materials (-1.03%) and consumer staples (-0.39%) segments weighed on returns.

Although stocks broadly remained attractive from a bottom-up perspective, investors began to face a conundrum of what may lie ahead for equity markets. The U.S. economy remained solid but continued to show growing signs of late-stage expansion. Additionally, concerns around price-to-earnings contraction, higher bond yields, and the negative impact of a strengthening U.S. dollar on emerging markets added to increased levels of general market anxiety.

### PERFORMANCE

The Mid-Cap Value Equity Composite's return of 3.55% (gross)/3.36% (net) outperformed the 3.30% return of the Russell Midcap Value Index. Stock selection and overweight positions in the industrials and healthcare sectors and an underweight position in consumer discretionary contributed to outperformance. Stock selection in the materials, financials, and energy sectors detracted from returns.

Humana and Zimmer Biomet Holdings were among the strongest stock contributors.

- Health insurance company Humana rose on higher-than-expected earnings and upbeat forward-looking guidance. The stock has been a consistently strong performer and continues to offer very attractive fundamentals, including an extremely healthy balance sheet and steady growth from Medicare Advantage enrollment increases driven by aging U.S. demographics.
- Medical device company Zimmer Biomet Holdings climbed on positive sector momentum, stronger-than-expected earnings, and a general rebound after being oversold on regulatory concerns. The firm also saw market share stabilization and continued to benefit from strong management under its new CEO.

### PORTFOLIO

CHARACTERISTICS	Portfolio	Benchmark
Market Cap (\$b)	17.73	14.93
Dividend Yield (%)	2.10	2.14
Price-to-Earnings*	19.88	16.93
Price-to-Book	2.26	1.99
Price-to-Sales	1.30	1.55
Std. Dev. (3 yr) (%)	10.30	9.62
Alpha (3 yr) (%)	2.24	0.00
Beta (3 yr)	1.03	1.00
Std. Dev. (5 yr) (%)	10.71	9.69
Alpha (5 yr) (%)	-0.10	0.00
Beta (5 yr)	1.06	1.00

\*P/E is calculated using trailing 12-month earnings.

TOP RELATIVE CONTRIBUTORS <sup>1,2</sup> (%)	Avg. Wgt.	Rel. Cont.
Zimmer Biomet Holdings, Inc.	3.60	0.60
Humana Inc.	3.96	0.56
Hubbell Inc. Class B	1.79	0.48
Motorola Solutions, Inc.	3.09	0.37
AmerisourceBergen Corp.	3.56	0.34

TOP RELATIVE DETRACTORS <sup>1,2</sup> (%)	Avg. Wgt.	Rel. Cont.
Martin Marietta Materials, Inc.	2.62	-0.51
Affiliated Managers Group, Inc.	2.36	-0.23
Anadarko Petroleum Corp.	0.63	-0.18
Noble Energy, Inc.	1.42	-0.16
Schneider National, Inc. Class B	1.60	-0.15

Rel. Cont. = contribution to return relative to benchmark.

### TOP 10 HOLDINGS<sup>1</sup> (% of Portfolio)

AmerisourceBergen Corp.	4.03
Zimmer Biomet Holdings, Inc.	3.86
Motorola Solutions, Inc.	3.74
Humana Inc.	3.64
Perrigo Co. Plc	3.50
Pinnacle Financial Partners, Inc.	2.76
Martin Marietta Materials, Inc.	2.64
Affiliated Managers Group, Inc.	2.61
Stanley Black & Decker, Inc.	2.50
Hartford Financial Services Group, Inc.	2.38

<sup>1</sup> See Holdings Disclosure on page 3.

<sup>2</sup> The contributors/detractors listed do not represent all securities purchased or sold for our clients. To obtain a list showing the contribution of each holding that contributed to overall performance during the quarter and the calculation methodology, please call 1-407-674-1270.

All data as of 9/30/18. Source: FactSet.

Martin Marietta Materials and Affiliated Managers Group were among the largest stock detractors.

- Building material supplier Martin Marietta Materials fell on weather concerns. The company does considerable business in Texas and North Carolina, and the wet spring and summer in Texas, followed by Hurricane Florence in North Carolina (which forced a temporary operations shutdown), both weighed on shares. We added to our position on the price weakness, as we see the slowdown as transitory. We continue to be enthusiastic about the firm's solid pricing power and the strong, longer-term tailwind of higher continued spending on aging infrastructure.
- Despite strong earnings and revenue, asset manager Affiliated Managers Group declined on general weakness and continued pricing pressures in the active investment management segment. We believe the stock has been oversold and have been slowly adding to our position, as the company offers a solid, well-diversified product line, with an excellent balance sheet and a proven track record of delivering strong results.

## PORTFOLIO CHANGES

The portfolio initiated positions in Zions Bancorporation and Devon Energy and exited MB Financial and Anadarko Petroleum.

- Bank holding company Zions Bancorporation is a new holding purchased for its strong fundamentals, including attractive excess capital, prudent credit underwriting, and an experienced management team focused on capturing steady shareholder returns.
- We bought gas exploration and production (E&P) company Devon Energy, which should benefit from higher commodity prices. We also view as favorable the firm's commitment to being a "pledger," which refers to a recent trend among E&P companies to introduce sounder business metrics that focus more intensely on invested capital return and rewarding investors than has been typical in the past. As such, Devon has announced plans to sell non-core assets to help fund a large share repurchase.
- We exited gas E&P company Anadarko Petroleum, which had been a solid performer for the portfolio but had begun to lag as it wavered on its "pledger" commitment.
- We sold bank holding company and long-term holding MB Financial when shares rallied on the announcement it planned to be acquired by Fifth Third Bancorp.

## PERFORMANCE ATTRIBUTION (%) AS OF 9/30/18

	Quarter-end Sector Weights		Impact		
	Portfolio	Benchmark	Sector Weight	Stock Selection	Total
Consumer Discretionary	4.69	11.38	0.17	-0.02	0.15
Consumer Staples	4.17	4.91	0.05	-0.13	-0.08
Energy	9.36	7.90	0.02	-0.31	-0.29
Financials	16.88	17.54	0.01	-0.33	-0.32
Health Care	15.04	6.84	0.48	0.21	0.69
Industrials	13.70	12.58	0.18	0.29	0.47
Information Technology	11.57	9.32	0.07	0.08	0.15
Materials	4.82	6.11	0.02	-0.44	-0.42
Real Estate	9.39	12.72	0.07	0.05	0.11
Telecomm Services	0.00	0.62	-0.07	0.00	-0.07
Utilities	10.39	10.08	0.02	-0.06	-0.04
Total			1.00	-0.65	0.36

**Overweight/Positive, Neutral, Underweight/Negative**

Source: FactSet.

Performance attribution does not incorporate the effects of cash, unclassified securities, or expenses and may change at any time without notice. The total impact may not equal the difference between Portfolio and Benchmark returns.

## OUTLOOK

In our view, it is stock fundamentals that matter most in the current market. While we remain bullish on the overall economy and see further upside potential in stocks, particularly in the companies we own, mounting signs of late-cycle pressures and the general increase in investor anxiety warrant a degree of caution—especially at today's higher valuations. Investors should also expect that stocks will continue to be more severely punished for results that miss market expectations than rewarded for beating them. In this type of environment, we believe it is imperative to keep risk exposure tightly controlled.

## PERFORMANCE COMPARISON (%) AS OF 9/30/18

	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Mid-Cap Value Equity Composite (Gross)	3.55	7.11	12.60	15.94	11.16	13.43
Mid-Cap Value Equity Composite (Net)	3.36	6.52	11.77	15.08	10.33	12.68
Russell Midcap® Value Index	3.30	3.13	8.81	13.09	10.72	11.29
eVestment Alliance Midcap Value Median*	3.10	3.97	9.07	13.10	10.62	11.77
# of Portfolios in Median Calculation	116	116	116	115	112	95

eVestment Alliance data capture date: 10/22/18

**Past performance is not indicative of future results.** This presentation is solely for SUPPLEMENTAL INFORMATION purposes, intended for institutional investors and may not be provided unless accompanied or preceded by the fully compliant GIPS Composite Presentation. The comparative performance contained herein reflects annualized returns for specific time period, are not indicative of actual annual returns, and may not be relied upon for investment decisions. Complete information regarding Ceredex's returns are included on the GIPS presentation on page 4. The performance inception date for the composite is 4/1/02.

Russell Midcap® Value Index is an unmanaged index which measures the performance of those securities found in the Russell Midcap universe with lower price-to-book ratios and lower forecasted growth values. The stocks are also members of the Russell 1000 Value index. Investors cannot invest directly in an index.

Frank Russell Company is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell® is a trademark of Frank Russell Company.

This information and general market-related projections are based on information available at the time, are subject to change without notice, are for informational purposes only, are not intended as individual or specific advice, may not represent the opinions of the entire firm, and may not be relied upon for individual investing purposes. Information provided is general and educational in nature, provided as general guidance on the subject covered, and is not intended to be authoritative. All information contained herein is believed to be correct, but accuracy cannot be guaranteed. This information may coincide or conflict with activities of the portfolio managers. It is not intended to be, and should not be construed as investment, legal, estate planning, or tax advice. Ceredex Value Advisors does not provide legal, estate planning or tax advice. Investors are advised to consult with their investment professional about their specific financial needs and goals before making any investment decisions. Portfolio characteristics, sector analysis, and holdings exclude cash and may change at any time without notice.

\*eVestment Alliance (eA) is a manager-reported database on hundreds of investment managers and thousands of investment products covering a full range of asset classes, investment styles, and geographic concentrations. Based on manager input, eA independently constructs universes using qualitative and quantitative factors. The investment products are organized into peer groups and assessed on an ongoing basis to ensure the consistency of a product's attributes within a designated style classification. In addition, eA utilizes style analysis tools, performance analytics, and the review of a product's investment strategy narrative in the construction of wide-ranging universes that are both pure in style and consistent over time.

The eVestment Number of Portfolios represents the number of investment products included in the calculation of the median return for the given eVestment universe for the given time period. Individual investment managers may have more than one investment product included in the universe, so the number of observations will likely be greater than the actual number of investment managers represented.

## HOLDINGS DISCLOSURE

The information provided in this report should not be considered a recommendation to purchase or sell any particular security. There is no assurance that any securities discussed herein will remain in an account's portfolio at the time you receive this report or that securities sold have not been repurchased. The securities discussed do not represent an account's entire portfolio and in the aggregate may represent only a small percentage of an account's portfolio holdings.

It should not be assumed that any of the securities transactions or holdings discussed were or will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein.

Dividends reflect past performance and there is no guarantee they will continue to be paid.

## IMPORTANT RISK CONSIDERATIONS

**Equity Securities:** The market price of equity securities may be adversely affected by financial market, industry, or issuer-specific events. Focus on a particular style or on small or medium-sized companies may enhance that risk. **Value Stocks:** Value stocks are subject to the risk that the broad market may not recognize their intrinsic value.

**For information, contact:**

Ceredex Value Advisors | 407-674-1270 | [www.ceredexvalue.com](http://www.ceredexvalue.com)

# Q3 | 2018 Mid-Cap Value Equity

MID-CAP VALUE EQUITY COMPOSITE 4/1/02 – 9/30/18

Year	Gross of Fee Return (%)	Net of Fee Return (%)	Benchmark Return (%)	Number of Portfolios	Composite Dispersion (%)	3-Year Standard Deviation		Total Composite Assets at End of Period (USD Millions)	Total Firm Assets (USD Millions)
						Composite	Benchmark		
2018 YTD	7.11	6.52	3.13	11	0.03	10.30	9.45	3,698	9,637
2017	12.75	11.91	13.34	11	0.14	11.55	10.32	3,664	10,095
2016	21.40	20.51	20.00	10	0.21	12.62	11.30	3,763	10,845
2015	-4.94	-5.65	-4.78	12	0.08	11.77	10.71	4,274	10,227
2014	12.26	11.33	14.75	12	0.06	10.83	9.81	5,027	12,269
2013	32.65	31.68	33.46	12	0.15	16.52	13.69	4,432	11,693
2012	23.07	22.15	18.51	9	N/A	20.63	16.76	2,857	8,740
2011	-6.31	-7.01	-1.38	4	N/A	23.75	22.78	1,940	6,493
2010	29.32	28.37	24.75	3	N/A	26.50	27.11	1,587	4,691
2009	48.43	47.68	34.21	3	N/A	23.53	25.01	696	3,082
2008	-33.72	-34.46	-38.44	3	N/A	19.32	18.74	254	2,116

**Ceredex Value Advisors LLC claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Ceredex has been independently verified for the period March 31, 2008 (the date of the Firm's founding) through December 31, 2017. A copy of the verification report is available upon request. 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 GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.**

- Ceredex Value Advisors LLC ("Ceredex") is an SEC-registered investment adviser and is a wholly owned subsidiary of Virtus Partners, Inc., a wholly owned subsidiary of Virtus Investment Partners, Inc. ("Virtus"). Registration of an investment adviser does not imply any level of skill or training. Ceredex manages assets on behalf of institutional and retail separate accounts and mutual funds. Ceredex became an affiliate of Virtus effective June 1, 2017, when Virtus acquired RidgeWorth Capital Management LLC and RidgeWorth Investments ("RidgeWorth"). Ceredex was created March 31, 2008, when all of the investment decision-makers associated with the value equity investment strategies of RidgeWorth became employees of Ceredex. The staff and decision making process remained intact and independent within Ceredex. For composite reporting purposes, the Firm is defined as all equity portfolios managed by Ceredex. Composite performance results are linked to performance history generated at RidgeWorth.
- The Mid-Cap Value Strategy composite includes all fully discretionary separately managed investment accounts and registered mutual funds managed in accordance with the mid cap value style with the objective of producing long-term capital appreciation and income. Under normal circumstances, Mid-Cap Value Portfolios will have at least 80% of their net assets invested in U.S. traded equity securities of mid-cap companies. U.S. traded equity securities may include American Depositary Receipts ("ADRs"). Ceredex considers mid-cap companies to be companies with market capitalizations similar to those of companies in the Russell Midcap Value Index. In selecting investments for the portfolios, Ceredex chooses companies that it believes are undervalued in the market relative to the industry sector and the company's own valuation history. Prior to September 1, 2015, the gross of fee return for the mutual fund was calculated by adding back the fund's published total operating expense ratio to the net of fee mutual fund performance; we now use the gross of fee return of the underlying portfolio. A complete description of the composite is available on request.
- The registered mutual fund was added to the composite effective April 1, 2008, immediately after the creation of Ceredex Value Advisors. Prior to that date the composite consisted of only separately managed accounts.
- The benchmark for the Mid-Cap Value Strategy composite is the Russell Midcap® Value Index. The Russell Midcap® Value Index is an unmanaged index which measures the performance of those securities found in the Russell Midcap universe with lower price-to-book ratios and lower forecasted growth values. The stocks are also members of the Russell 1000® Value Index. The index is calculated on a total-return basis with dividends reinvested. Index returns do not reflect the deduction of any fees or expenses.
- The three-year annualized standard deviations for the composite and the benchmark index are calculated using monthly returns.
- Valuations and returns are computed and stated in U.S. Dollars.
- Beginning March 31, 2008, composite policy requires the temporary removal of any portfolio incurring a client initiated significant cash inflow or outflow of 10% or greater of portfolio assets.
- The dispersion of annual returns is measured by the standard deviation across equal-weighted portfolio returns represented within the composite for the full year. No dispersion is reported for periods with five or fewer portfolios (shown as N/A).
- Returns are calculated based on total return which (a) includes cash returns, realized and unrealized gains plus income; (b) utilizes trade date and accrual accounting; and (c) is after the deduction of actual trading fees and expenses. Portfolio returns are calculated utilizing daily valuation. Composite returns, calculated monthly, are the weighted average return of the underlying portfolios using beginning-of-period market values. Composite gross of fee returns do not reflect any deduction for investment advisory fees, custodial charges or other costs that a client might incur in connection with the management of an account. Composite net of fee performance is calculated assuming a fee of 0.75%, the highest fee for this type of investment account.
- The standard management fee schedule applicable to mid-cap value accounts is as follows: 0.75% on the first \$25 million, 0.65% on the next \$25 million, 0.55% on the next \$50 million, and 0.50% on all over \$100 million. The minimum annual fee is \$15,000. Actual investment advisory fees incurred by clients may vary.
- This composite was created March 31, 2008, the inception date of Ceredex, and continues the investment strategy of a composite originally created in 2007. The composite has performance history with an inception date of April 1, 2002.
- The minimum portfolio size for the Mid Cap Value Strategy composite is \$1 million. For further information on investment management fees, please refer to Form ADV Part 2.
- Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.
- A complete list and description of firm composites and performance results is available upon request.
- Past performance is not indicative of future results and no investment is guaranteed for return of principal and/or return on investments. Results may vary among accounts. All information provided and used in calculations is believed to be correct, but accuracy cannot be guaranteed. Please consult with a financial professional before investing.