High Dividend Value Equity
Q4 2018 Commentary

Market Review:

Through the first three quarters of 2018, it appeared as though the US equity market was headed for another big year, as the S&P 500 was up over 10% to that point. However, the fourth quarter quickly erased those gains, with the S&P 500 finishing down 13.5% for the quarter and the Russell 1000 Value down 11.7%. It was the worst quarterly performance in ten years, since the depths of the financial crisis in the fourth quarter of 2008. The month of October turned out to be the worst-performing month since September 2011, and after a modestly positive November, the market finished the year with its worst December since 1931. The full-year 2018 turned out to be the worst year for US equities since 2008, with the S&P 500 down 4.4% for the year, despite the index EPS on track to increase approximately 20% from 2017. 2018 also ended the streak of nine consecutive years of positive returns for the S&P 500, which tied the longest streak in history since 1936.

On a sector basis, Energy was the worst performer, down 23.8%. The WTI oil benchmark, which began the quarter at a nearly four-year high of $75 per barrel, declined 38% to $45 on concerns of excess inventories in the midst of slowing global growth. Information Technology (-17.3%) was the next worst performer. After being up 38% in 2017, then another 25% through the first three quarters of 2018, Technology pulled back sharply as each component of the so-called FAANG index fell into bear market territory. Industrials (-17.3%) and Consumer Discretionary (-16.4%) were the next worst performers. Utilities (+1.4%) was the only sector to finish the quarter in positive territory, as it and other defensive sectors, including Real Estate (-3.8%) and Consumer Staples (-5.2%) outperformed. Health Care was the best performing sector for the year (+6.5%), benefitting from its defensive attributes and the perceived alleviation of regulatory scrutiny over high drug prices.

The fourth quarter was a reminder of how abruptly sentiment can shift, not only on stocks, but on the US economy. In early October Fed Chairman Jerome Powell telegraphed interest rates were “a long way from neutral”, noting that extremely accommodative monetary policy was no longer necessary. This statement alone appeared to spark investor anxiety. By November, Powell shifted course, stating rates were “just below” neutral, and by the December rate hike of 0.25% the Fed dot plot implied there would only be two raises in 2019. While few indicators point to an imminent recession in the US, tempered outlooks from prominent technology and industrial firms indicate increasing pockets of weakness. The market sell-off was also driven by fears of a potential trade war with China. With $250B of Chinese goods already subject to tariffs, the Trump administration said it was prepared to impose tariffs on all remaining Chinese imports, before both sides agreed to delay any further tariff actions for 90 days.

Heading into 2019, we believe political unrest will likely continue to weigh on global markets. In the US, this includes a partial Federal government shutdown over funding for a border wall, President Trump’s surprise announcement on a US troop withdrawal from Syria, and a newly Democratic-led House of Representatives sure to apply pressure on Trump. Internationally, we believe markets will continue to contend with significant uncertainty surrounding Brexit, conflict between President Emmanuel Macron and protesters in France, and a new President in Brazil, among a host of other issues.

Performance Analysis:

The S&P 500 returned -13.5% for the fourth quarter and -4.4% for the full year 2018 while the Russell 1000 Value returned -11.7% for the fourth quarter and -8.3% for the full year 2018.

The High Dividend Value Equity strategy composite returned -7.6% (gross) and -7.7% (net) for the fourth quarter and -3.3% (gross) and -3.7% (net) for the full year 2018, outperforming both the S&P 500 and Russell 1000 Value for the quarter and year.

Figure 1: High Dividend Value Equity Returns vs. Benchmark

	Q4	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Incept*
High Dividend Value Equity (gross)	-7.6	-3.3	-3.3	8.3	7.3	10.8	10.1
High Dividend Value Equity (net)	-7.7	-3.7	-3.7	7.8	6.9	10.3	9.5
Russell 1000 Value Index	-11.7	-8.3	-8.3	7.0	6.0	11.2	9.0
S&P 500 Index	-13.5	-4.4	-4.4	9.3	8.5	13.1	9.1

**December 31, 1993. Performance for periods greater than 1 year is annualized.*

The fourth quarter's heightened volatility and dramatic sell-off were led by deep Cyclicals and Technology stocks, in particular the FAANG index. While macroeconomic factors, namely slowing global growth, escalating China trade tariffs and normalizing monetary policy negatively impacted equity markets, the unwinding of algorithmic/high frequency trading positions also contributed to the steep slide. While Growth outperformed Value in 2018 by 680 basis points (Russell 1000 Growth – Russell 1000 Value returns), Value outperformed Growth by 420 basis points in Q4.

High quality (measured by balance sheet rating and profitability) and low beta stocks outperformed in Q4 amid the rising volatility; the flight to safety resulted in the US 10-year yield falling 36bps in the quarter to 2.69% at quarter end. The two highest dividend yielding quintiles delivered strong relative performance against the S&P 500, led by the Utilities, Real Estate and Consumer Staples sectors in the quarter.

The investment discipline core to the High Dividend Value Equity strategy focuses on the long-term factors that drive superior risk-adjusted returns – investments in high quality companies with attractive relative valuations, sustainable and growing dividends and catalysts to drive earnings growth and improving sentiment. Committing to this process over market cycles has rewarded clients with solid long-term gains and down market protection. At quarter-end:

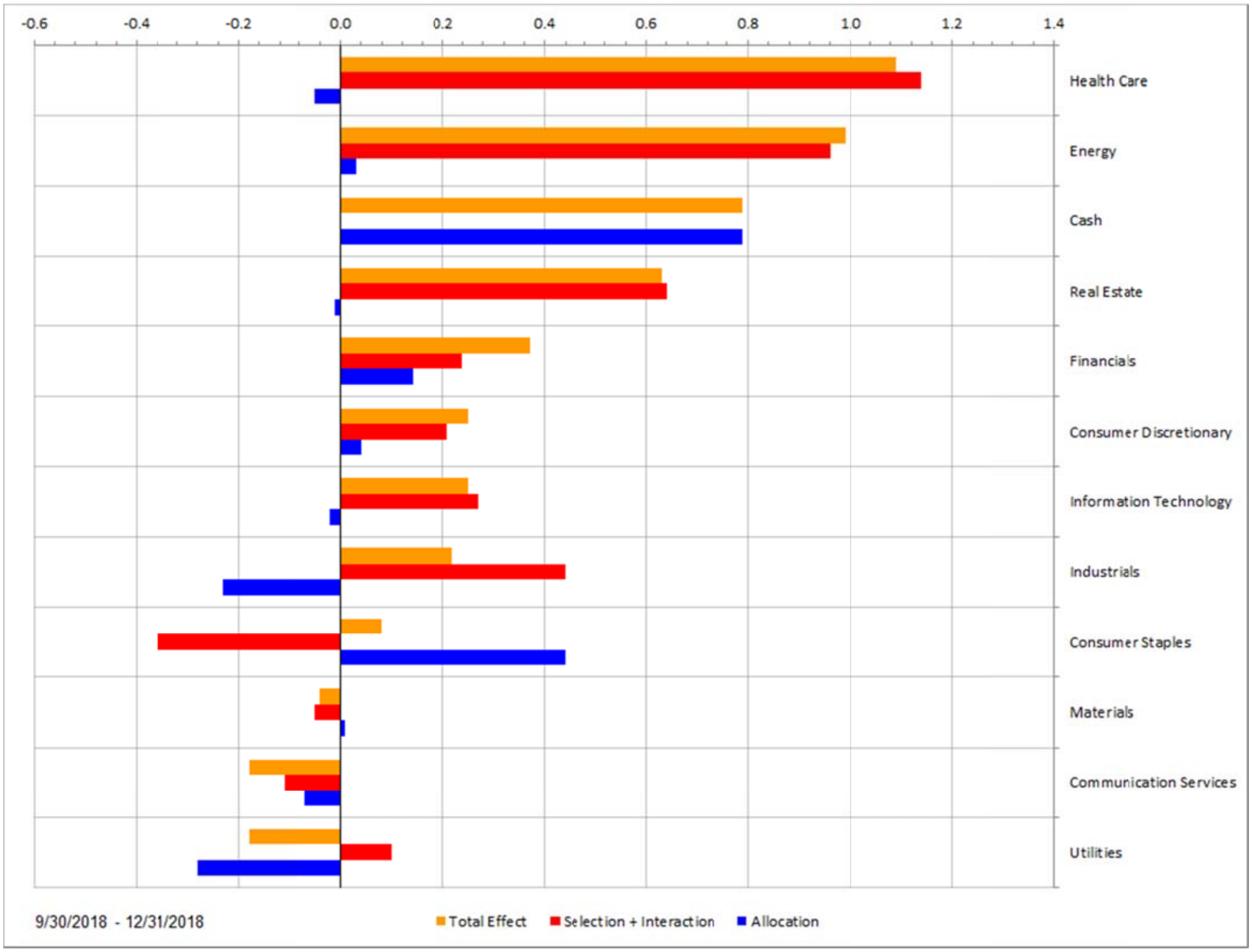
- **Low P/E Valuation Discipline**: The strategy's P/E is 14.1x 2019 earnings versus 16.5x for the S&P 500 and 15.2x for the Russell 1000 Value (Q4).

- **High Absolute Dividend Yield**: The strategy's dividend yield is 3.6% versus 2.4% for the S&P 500 and 2.7% for the Russell 1000 Value (Q4).

- **Strong Dividend Growth**: In Q4, 3 out of 37 portfolio companies raised their dividends with an average increase of 10.8%. In 2018, 31 out of 37 portfolio companies have raised their dividends with an average increase of +10.6%.

Portfolio Attribution:

Attribution Effects – High Dividend Value vs. Russell 1000 Value 9/30/2018 – 12/31/2018



Source: SCCM/Bloomberg, 12/31/2018.

The following attribution analysis of the High Dividend Value Equity portfolio utilizes the Russell 1000 Value as the benchmark of comparison for the fourth quarter of 2018.

Our strong stock selection made the ***Health Care*** sector the largest contributor to relative performance for the quarter. Merck (+8.5%) reported strong quarterly results with sales of its leading immuno-oncology drug, Keytruda, up 82% year-over-year. Eli Lilly (+8.4%), with its leading portfolio of diabetes drugs, saw sales of Trulicity increase 34% from last year and continues to execute on pipeline commercialization. Our underweight allocation combined with strong stock selection in the ***Energy*** sector aided relative performance. Energy was the worst-performing sector in the quarter as the WTI oil benchmark declined 38% to $45. Chevron (-10.2%) and Royal Dutch Shell (-14.25%), although down significantly, declined far less than the overall sector, helped in part by their integrated business models that make them less exposed to sharp swings in oil prices. Strong stock selection in the ***Real Estate*** sector aided returns as Welltower (+9.3%) and HCP (+7.5%) are both benefitting from restructured portfolios and a large demographic tailwind that should increase demand for health care properties in the coming years. Our underweight allocation and strong stock selection in ***Financials*** aided performance as the sector sold off sharply in December with a flattening yield curve threatening bank profitability. Chubb (-2.8%) reported strong premium growth in the third quarter combined with improved underwriting profit from a year ago, while HSBC (-5.4%) is benefitting from increased cost controls and strong loan growth in Asia. Our underweight allocation and strong stock selection in the ***Consumer Discretionary*** sector aided performance as retailers sold off despite record holiday season sales, and Genuine Parts' (-2.7%) automotive division reported its highest comparable sales growth in almost three years. Finally, the portfolio benefitted from our strong stock selection in ***Information Technology***, as Intel (-0.1%) reported both revenue and earnings above expectations, driven by strong growth in its data center and PC businesses.

Our underweight allocation to the ***Utilities*** sector detracted from relative performance, as the defensive sector was the only sector to finish the quarter in positive territory. However, our holding in NextEra (+4.4%) outperformed, as its renewable power generation business continues to expand and its regulated utility increased earnings from the prior year. Our underweight allocation to the newly formed ***Communication Services*** sector detracted from relative performance. However, our position in BCE (-1.1%) outperformed as the company reported strong results particularly in its Wireless unit. Stock selection in ***Materials*** detracted from relative performance, as DowDuPont (-16.3%) declined partly due to an impairment charge related to its Agriculture business; however, following the split-up of the company in 2019, each of its three businesses are expected to be more focused with improved capital allocation profiles.

Portfolio Changes:

Purchases / Additions

There were no new investments in the quarter. The position in **DowDupont** was raised in the strategy.

Sales / Reductions

Metlife (MET) was sold from the High Dividend Value strategy. Since the financial crisis, Metlife's management team has sought to sell non-core businesses and improve earnings stability. However, the company's business is now more focused on low growth markets (life insurance and protection policies) that have a high degree of interest rate sensitivity. While higher rates have historically increased life insurance investment income, funding costs are rising and long-term rates must increase significantly from here to boost earnings. In addition, given the company's significant exposure to credit in its investment portfolio, risks from higher investment losses and credit spread widening are increasing. The management team has failed to deliver the earnings growth and dividend growth consistency that we expect and for these reasons we decided to exit the position.

Dividend Summary:

In the fourth quarter of 2018, 3 out of 37 portfolio companies raised their dividend payments with an average increase of +10.8%:

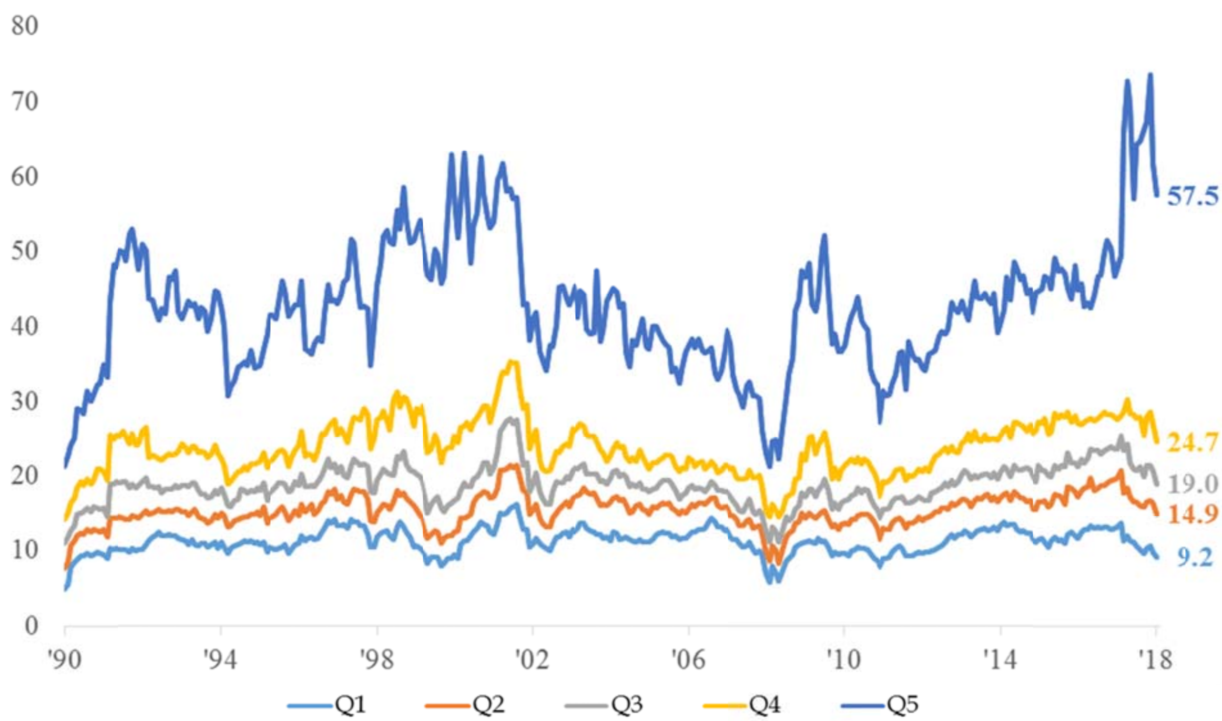
- ConocoPhillips (COP) raised its dividend payment by +15.1%
- Merck (MRK) raised its dividend payment by +14.6%
- Siemens (SIEGY) raised its dividend payment by +2.7%

In 2018, 31 out of 37 portfolio companies have raised their dividends with an average increase of +10.6%.

Market Outlook:

Strong US economic data and robust corporate earnings growth in Q4 took a backseat to the market's increasing concerns on slowing global growth, the China trade war and normalizing monetary policy. The risk-off environment in 2018 resulted in 90% of major asset classes posting a negative return, versus the historical average of 29%, a pattern not experienced since 1921. While S&P 500 index earnings are expected to be up over 20% for 2018, with the index price decline, the Price/Earnings multiple fell 22%. Valuation multiples compressed the greatest for deep cyclicals (Energy, Financials, Industrials) and the least for stable sectors (Health Care, Utilities). The rapid market sell-off and elevated volatility have presented an increasing number of attractive investment opportunities not seen for quite some time. However, the dispersion in valuation multiples remains high – a number of industries are trading at recession-like multiples while Growth stock valuations remain high. In past cycles, heightened volatility has historically led to multiple compression driven by the highest multiple stocks[1]. Even with the recent underperformance of Growth relative to Value stocks, the valuation of Growth stocks are at extreme levels relative to historical averages.

Figure 2: S&P 500 Median Trailing P/E By Quintile



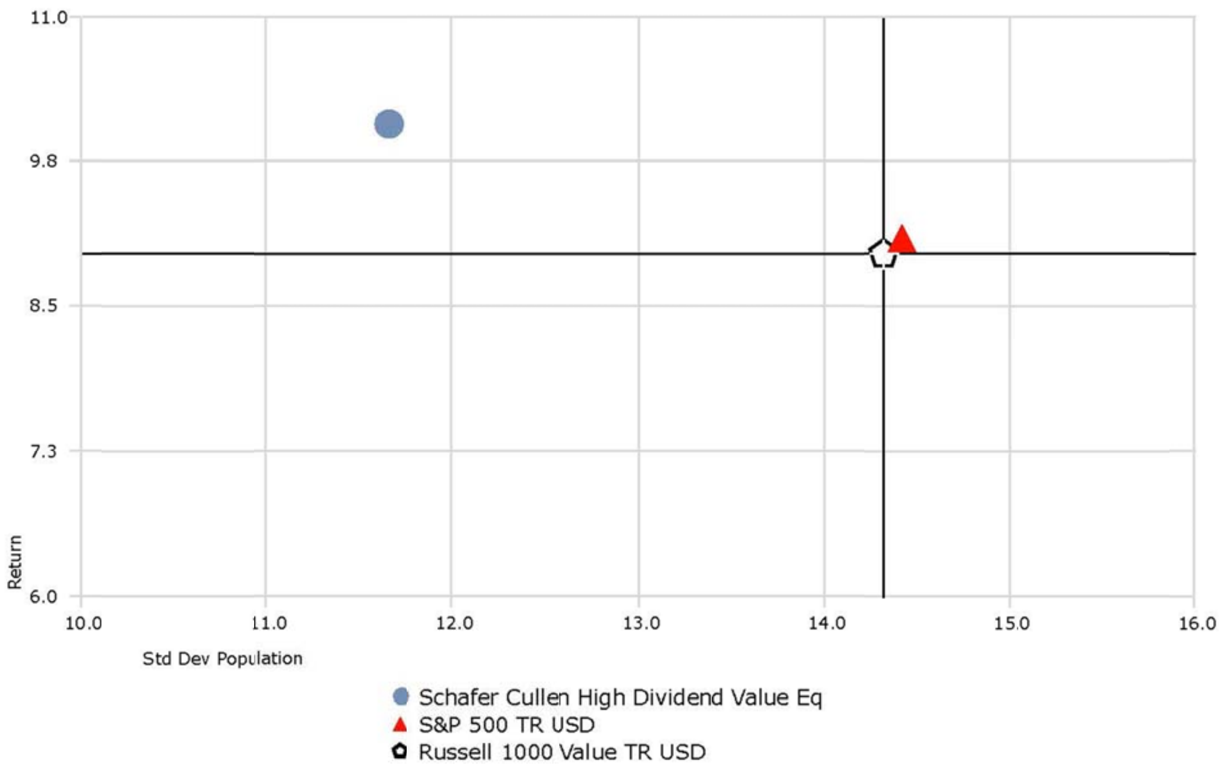
Source: Strategas Research, 12/31/2018.

A headwind to global equities has been the tightening of monetary policy by world central banks. At year-end 2018, 56% of developed and emerging market central banks were tightening policy (30+ countries), the largest proportion in seven years. Historically, equities tend to deliver lower returns when more than half of the world's central banks are tightening policy[2]. In addition, the Federal Reserve's balance sheet run-off (quantitative tightening) continues to drain excess liquidity with the real global monetary base currently contracting 1% and projected to further contract by 4%+ by December 2019 if the Fed's current target of nearly $500B in assets roll off and the ECB and BOJ maintain assets at current levels. However, with global growth decelerating, central banks are already looking to adjust monetary policy, helping to stabilize global equities.

[1] Bernstein Research, "US Portfolio Strategy", December 2018.
[2] Ned Davis Research, "Global Monetary Tightening Hurting Equities", December 2018.

Fundamentally, in our view the prospect for US equities in 2019 appears positive, supported by a mid- to high-single digit year-over-year growth in S&P 500 earnings, relatively attractive valuation multiples and market sentiment coming off extreme levels. However, the current economic recovery's record length and the stark divergence between the economic recovery and financial recovery since 2009 should be considered. Nominal GDP growth in this cycle has been one of the weakest since the 1930's while equity market returns have been one of the strongest driven in part by unprecedented stimulus and aggressive monetary easing and a record level of share repurchases estimated at $4.5T in the US corporate sector. With less stimulative monetary policy and rising sovereign and corporate debt levels, the wide dispersion between asset price inflation and real economy inflation are at risk of convergence. In this environment, risk-adjusted returns are likely to adjust to more normalized levels and strategies that have delivered superior risk-adjusted returns through market cycles become even more critical.

Figure 3: SCCM High Dividend Value Since Inception Total Risk Reward



	Return	Std Dev Population	Alpha	Beta	R2	Sharpe Ratio	Information Ratio (arith)	Tracking Error	Down Capture Ratio	Up Capture Ratio
Schafer Cullen High Dividend Value Eq	10.08	11.65	2.50	0.75	84.54	0.67	0.19	5.84	68.87	84.00
S&P 500 TR USD	9.07	14.43	0.50	0.95	88.58	0.50	0.03	4.94	96.33	98.07
Russell 1000 Value TR USD	8.95	14.32	0.00	1.00	100.00	0.50	–	0.00	100.00	100.00

Source: Morningstar Direct, 12/31/2018

Thank you for your continued support. Feel free to reach out to us if you have any questions.

Best Regards,
Schafer Cullen Capital Management, Inc.

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The S&P 500 Index is a market capitalization-weighted index of 500 companies in leading industries of the US economy. The index is unmanaged and has no fees.
The Russell 1000 Value Index measures the performance of the large-cap value segment of the US equity universe.
It includes those Russell 1000 companies with lower price-to-book ratios and lower expected and historical growth rates. One cannot invest directly in an index.

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