High Dividend Value Equity
Q2 2019 Commentary

Market Review:

US equities had a volatile second quarter, but the S&P 500 finished up 4.3% and the Russell 1000 Value returned 3.8% to end the month of June at near record price levels. The S&P 500 also posted its best first half in 22 years (1997), up 18.5%. The quarter saw an extension of the major themes that sparked volatility over the past three quarters, namely the US-China trade dispute and the Federal Reserve's shifting interest rate policy. Stocks were up significantly in April, extending the rally that began at the end of December when the Fed began shifting to a more accommodative stance on interest rates. However, the market retreated sharply in the month of May when trade negotiations deteriorated and concerns grew over a lengthened dispute. Stocks recovered quickly with the best month of June for the S&P 500 since 1955, largely on hopes of interest rate cuts by the Fed.

Returns in the quarter were broadly distributed, with 10 of the 11 sectors finishing in positive territory. Financials (+8.0%) was the best-performing sector, driven by optimism for a global cyclical recovery in back half of the year and finished the quarter strong with the Fed's approval of large capital return plans for most of the largest banks. Materials (+6.3%) was the next best performing sector, as gold stocks soared on increasing Fed rate cut expectations. Information Technology was up +6.1%, with software and IT services companies outperforming. Energy was the only sector that posted a negative return (-2.8%), as the WTI oil benchmark declined on concerns of reduced demand from slowing global growth. Health Care (+1.4%) was also a laggard, impacted by increasing political rhetoric on health care reform and various drug pricing initiatives.

Concerns grew on US-China trade when Treasury Secretary Steven Mnuchin announced that talks had gone "substantially backward," and the Trump Administration soon levied a new 25% of tariffs on $200B of Chinese imports while threatening additional measures. China President Xi Jinping retaliated with tariffs on $60B of US imports; furthermore, the Xi administration appeared to take a much harder long-term stance on trade, indicating through several statements and other actions that the country is prepared to negotiate for an extended period if necessary. Concurrently, President Trump threatened to levy tariffs on Mexico unless the Mexican government took action to deter the flow of Central American migrants passing through its borders. Ultimately, The Trump administration reached an agreement with Mexico, and on the final day of the quarter Trump and Xi reached some concessions and an agreement to restart talks.

Yields on US government bonds continued to decline, reflecting concerns over slowing global growth and increased demand for safe haven assets. Although the US economy surprised with 3.1% GDP growth for the 1st quarter, the IMF lowered its projection for global growth to 3.3% in 2019, down from 3.6% in 2018. The 10-year US Treasury yield dipped below 2% and has fallen by more than a full percentage point over the past three quarters. Notably, the 10-year yield also dipped below the yield on short-term Treasurys, resulting in an inverted yield curve; however, most economists dismissed the likelihood of an impending recession.

Performance Analysis:

The High Dividend Value Equity strategy composite returned 1.6% (gross) and 1.5% (net) for the second quarter of 2019. The strategy underperformed the S&P 500 and Russell 1000 Value for the quarter.

Figure 1: High Dividend Value Equity Returns vs. Benchmark

	Q2	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Incept*
High Dividend Value Equity (gross)	1.6	13.2	11.7	10.1	8.3	13.0	10.4
High Dividend Value Equity (net)	1.5	13.0	11.3	9.7	7.8	12.5	9.8
Russell 1000 Value Index	3.8	16.2	8.5	10.2	7.5	13.2	9.4
S&P 500 Index	4.3	18.5	10.4	14.2	10.7	14.7	9.6

**12/31/ 1993. Performance for periods greater than 1 year is annualized. Past performance is no guarantee of future results.*

The quarter saw several narrative changes with an initial "risk-on" environment in April led by Growth and Cyclicals, followed by a "risk-off" rotation into Defensives in May and finally a euphoric June back into high beta sectors. Growth continued its outperformance over Value by 80 basis points in the quarter (Russell 1000 Growth – Russell 1000 Value) and 525 basis points for the year. Yield sectors underperformed in the quarter with the two highest yielding dividend quintiles underperforming in the quarter and year-to-date:

Figure 2: S&P 500 Price Performance by Dividend Quintile

	# of	Wgt in	Absolute Price Performance					BofAML	Proj EPS Growth		Forward	Div.
	Comp	S&P 500	1 Mon	3 Mon	6 Mon	12 Mon	YTD	Adj Beta	2018	2019	P/E Ratio	Yield
Yield Sectors												
0.00 To 0.31	101	22.03	5.65	4.55	20.26	4.99	20.26	1.09	10	14	22	0.01
0.31 To 1.52	101	15.14	7.80	3.48	19.94	3.78	19.94	1.05	10	13	21	1.01
1.52 To 2.36	101	24.95	8.12	6.13	21.13	17.48	21.13	1.02	4	11	16	1.88
2.36 To 3.32	101	19.14	6.08	3.34	13.39	9.82	13.39	0.95	5	8	15	2.78
3.32 To 16.24	101	18.74	7.01	0.73	12.59	4.87	12.59	0.91	-1	7	12	4.50
S&P 500	505	100.00	6.89	3.79	17.35	8.22	17.35	1.01	5	10	16.70	1.97

Source: Bank of America Merrill Lynch, 6/30/2019. Past performance is no guarantee of future results.

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:

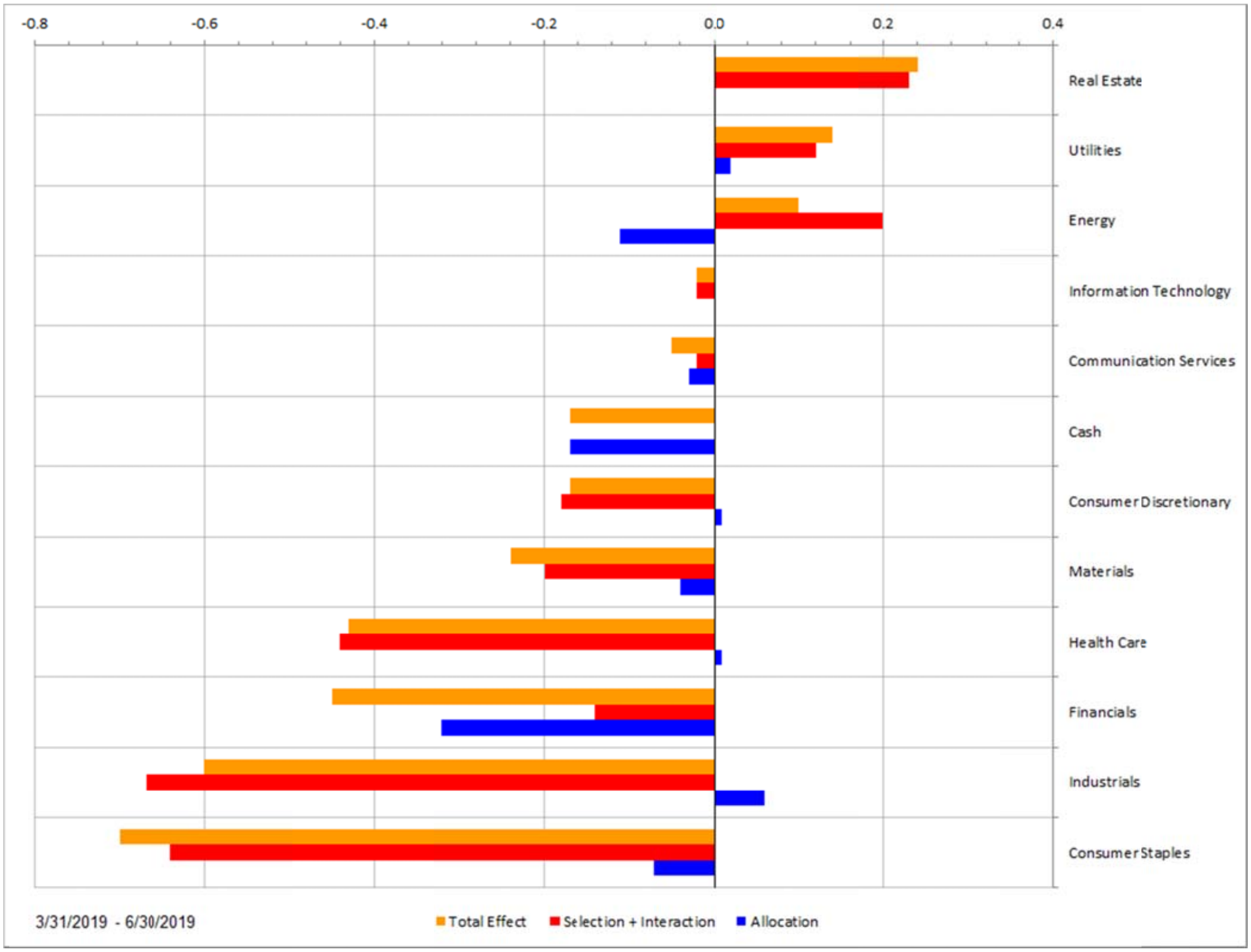
- **Low P/E Valuation Discipline**: The strategy's P/E was 16.1x 2019 earnings versus 19.2x for the S&P 500 and 17.4x for the Russell 1000 Value (Q2).

- **High Absolute Dividend Yield**: The strategy's dividend yield was 3.4% versus 2.1% for the S&P 500 and 2.6% for the Russell 1000 Value (Q2).

- **Strong Dividend Growth**: In Q2, 6 out of 40 portfolio companies raised their dividends with an average increase of 5.0%.

Portfolio Attribution:

Attribution Effects – High Dividend Value vs. Russell 1000 Value 3/31/2019 – 6/30/2019



Source: SCCM/Bloomberg, 6/30/2019.

The following attribution analysis of the High Dividend Value Equity portfolio utilizes the Russell 1000 Value Index as the benchmark of comparison for the second quarter of 2019.

Our underweight allocation and strong stock selection made ***Real Estate*** the largest contributor to relative performance. Real Estate underperformed as defensive sectors lagged in the quarter. Welltower (+6.2%) reported strong 1st quarter earnings, as its seniors housing portfolio posted net operating income growth above consensus estimates and also reported strong growth in its post-acute and medical office building portfolios. HCP (+3.4%) also reported positive earnings results, as growing demand in particular for its life sciences properties continues to drive growth in net operating income. Our underweight allocation and stock selection in ***Utilities*** aided performance, as the defensive sector lagged and NextEra Energy (+6.6%) outperformed. NextEra management extended its growth outlook to 2022 for its regulated utility, Florida Power & Light, and its independent power producer, NextEra Energy Resources, as both entities continue to benefit from growth in renewable energy. Stock selection within the ***Energy*** sector aided performance as Royal Dutch Shell (+4.3%) increased its long-term free cash flow targets through 2025, which should sustain its planned capital returns to shareholders. Chevron (+2.0%) outperformed as it terminated its bid for Anadarko Petroleum, seeing substantial growth in production from the Permian Basin and from its LNG projects in Australia.

Our overweight allocation and stock selection within the ***Consumer Staples*** sector detracted from relative performance. Altria (-16.3%) underperformed on concerns of accelerating volume declines and potential regulatory action by the FDA; however, the company is raising prices at an accelerated rate and investing in various reduced risk products to help offset combustible volume declines. Walgreens Boots Alliance (-12.9%) declined after management lowered earnings guidance for the year, although the company ended the quarter on a strong note as it reported quarterly earnings ahead of consensus estimates helped by strong retail pharmacy sales growth. Within ***Industrials***, 3M (-15.9%) declined on lower-than-expected earnings stemming from weakness in the automotive and electronics industries in China and Japan. Boeing (-4.0%) underperformed on continuing uncertainty surrounding the 737 MAX; however, the company received an order from International Airlines Group for 200 737 MAX aircraft at the Paris Air Show. Our underweight allocation and stock selection within ***Financials*** detracted from relative performance as Financials was the best-performing sector, largely driven by optimism on a global cyclical recovery. Wells Fargo (-1.1%) lagged in the quarter but was approved by the Fed to repurchase up to $23B in stock, or roughly 11% of its market capitalization, while increasing its quarterly dividend 13%.

Portfolio Changes:

Purchases / Additions

Bank of America (BAC): A position in Bank of America was established in the quarter. Bank of America, one of the largest US banks by assets and branch network, offers consumer banking, credit cards, mortgage lending, corporate and investment banking and asset management services through its Merrill Lynch and US Trust platforms. The company is one of the most diversified, high quality banks with strong long-term growth prospects; BAC has built significant scale in each of its businesses, focusing on driving new areas of top-line growth while improving underwriting, efficiency and strengthening its balance sheet. The Consumer banking business is experiencing solid loan growth with a strong funding base, holding the highest deposit market share in the country, and maintaining high credit quality (with an average FICO score of 770). The bank's Investment Banking division has invested heavily in technology to grow its Trading business and focused on gaining market share in M&A/Advisory. The Wealth and Investment management business, the company's crown jewel, consists of Merrill Lynch and US Trust, continues to increase its fee-based model and deliver peer leading margins. Management, led by Brian Moynihan, has been focused on making significant investments in technology and operational efficiency to lower operating costs, improve the customer experience and gain market share. The annual Fed stress test results (DFAST), which evaluates capital levels under various economic downturn scenarios, were recently released and Bank of America's projected capital levels came in significantly above minimum requirements for all five capital ratio requirements. As a result of its positive outcomes, the company announced a 2019 CCAR cycle capital plan with $30.9B in gross share repurchases, roughly 11.5% of its market capitalization, and a 20% increase in its quarterly dividend.

Banks have underperformed the market over the past 2.5 years and are one of the more attractively-valued segments of the market; however, considering the group's higher beta nature and historical underperformance in downturns, they generally trade at a discount to the market. In late 2016, the prospect of corporate tax reform, the loosening of financial regulations and a steeper yield curve propelled bank stocks higher. Since then, large banks have faced the headwind of a flatter yield curve pressuring net interest margins (NIM) and no significant regulatory relief is in sight. Despite the flattening/inverted yield curve, banks stocks have begun to stabilize and are already pricing in Fed rate cuts over the next several quarters. Bank of America trades at 9x forward earnings, 1.0x book value with a 2.7% dividend yield at purchase.

Siemens (SIEGY): The position in Siemens was raised in the quarter. Siemen's short-cycle automation and long-cycle capital goods businesses are performing well in the midst of a more uncertain macro environment given the company's product focus on improving industrial productivity and energy efficiency. In addition, we believe management's actions to focus the company's portfolio on secular growth markets where it has leading market share and divesting/spinning out non-core businesses will sharpen management's focus, improve returns and potentially lift the stock's valuation.

SunTrust (STI): The position in SunTrust was raised in the quarter. The significant sell-off in Financials in May left valuations on bank stocks, including SunTrust, increasingly attractive. We believe the SunTrust/BB&T merger integration and savings will provide earnings accretion support in a tougher economic environment and position the combined company well in one of the fastest growing parts of the US.

Corning (GLW): The position in Corning was raised in the quarter. The May sell-off in Technology provided an attractive entry point for Corning. We believe the company's dominant display business remains resilient while its Environmental Technologies and Optical Communications (fiber) businesses are positioned well for secular growth in emissions control and 5G deployment.

Target (TGT): The position in Target was raised in the quarter. The company is benefitting from its digital investments and store fulfillment model as well as the consolidating retail industry to gain market share. While Amazon continues to offer faster delivery, Target's menu of fulfillment options as well as its strong merchandizing strategy are attracting consumers to their physical stores.

Intel (INTC): The position in Intel was raised in the quarter. Intel has a dominant position in the PC and server markets with a number of emerging growth verticals in automotive mobility, internet of things and communications equipment. New CEO Bob Swan is providing more financial discipline to the company through implementing operating efficiencies and optimizing business mix and investments.

Dow (DOW): The position in Dow was raised in the quarter. Dow is a leading specialty chemical company with cost-advantaged asset base, primarily in North America which benefits from low cost shale resources. After its split from DuPont, the company is seeking to improve financial returns through operational efficiencies and increased scale.

Sales / Reductions

Alcon (ALC): Alcon, a spin-off from Novartis, was sold in the quarter. Alcon, a leading supplier of eye care products including surgical equipment, contact lenses and refractive technology products, has solid growth prospects after a multi-year turnaround phase including R&D investments. However, the stock trades at an expensive valuation: 31x 2019 EPS with a 0.2% dividend yield.

Altria (MO): The position in Altria was reduced in the quarter. Altria is facing steeper declines in its core combustibles cigarette business as volume declines have worsened, partially offset by improved pricing. The benefit from its stakes in JUUL (e-Cigarette), Cronos (cannabis) and its joint venture with Phillip Morris International on IQOS (heat-not-burn cigarette alternative) will help Altria to grow in these new markets however at the risk of cannibalizing its most profitable core business with less favorable economics. While Altria's attractive valuation and yield, trading at 11.5x 2019 earnings and a 6.6% dividend yield, already discount these risks, the uncertainty facing the company give us some degree of caution.

Dividend Summary:

In the second quarter of 2019, 6 out of 40 portfolio companies raised their dividend payments with an average increase of 5.0%:

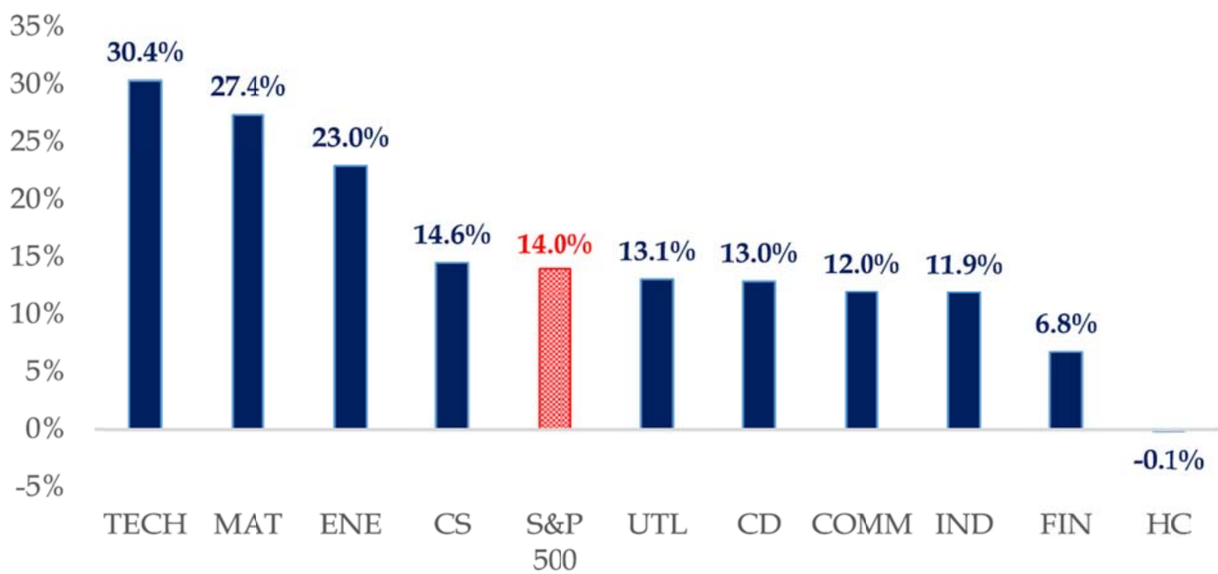
- Chubb (CB) raised its dividend payment by +2.7%
- Exxon Mobil (XOM) raised its dividend payment by +6.1%
- Johnson & Johnson (JNJ) raised its dividend payment by +5.6%
- Target (TGT) raised its dividend payment by +3.1%
- Travelers (TRV) raised its dividend payment by +6.5%
- Unilever (UN) raised its dividend payment by +6.0%

Year-to-date, 22 out of 40 portfolio companies have raised their dividends with an average increase of 6.2%. This builds on the strength of 2018 where 31 out of 37 portfolio companies raised their dividends with an average increase of +10.6%.

Market Outlook:

The equity market rally to record highs by the end of the second quarter was driven by a significant turn in global central banking policy with the Federal Reserve now expected to cut interest rates this year, as a result of weakening US economic data and macro uncertainties including the outcome of the US-China trade war and the impact of the tariffs on the economy. The current state of "bad news is good news" for the market is evidenced by the flattening yield curve alongside peak equity levels. Valuation expansion has accounted for nearly all of the rally year-to-date as earnings expectations have continued to decline throughout the year.

Figure 3: S&P 500 Change in Price/Earnings Ratio (1/1/2019 - 7/1/2019)

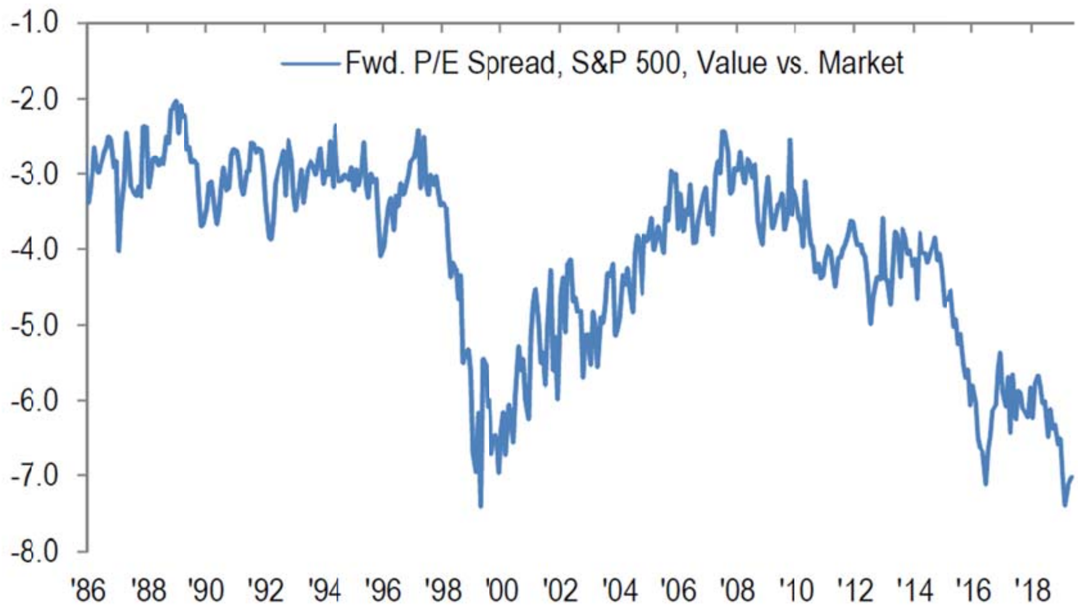


Source: Strategas, Quarterly Review in Charts, 7/1/2019. The graph is for illustrative purposes only and does not reflect information about any fund or other account managed or serviced by Schafer Cullen Capital Management.

At this juncture, the global slowdown may simply be a "soft patch" or a deeper mid-cycle slowdown. This uncertainty caused US yields to fall precipitously in the quarter and the S&P equity risk premium (Earnings Yield less 10-year Treasury Yield) rose to 320 basis points, 1 standard deviation above the long-term average. However, with overall growth expectations declining, the current increase in the ERP may be justified. Since January 2019, S&P 500 consensus earnings estimates for 2019 have declined nearly 6% to +8% year-over-year (Ned Davis Research, June 2019). Meanwhile, equity markets have been relatively range-bound over the past 18 months as “risk off” (Growth and Defensive) outperforms on the slowdown narrative while “risk on” (Financials and Cyclicals) outperforms on a recovery narrative. With markets now pricing in an imminent recovery, the question is whether renewed monetary easing will be enough to offset broadly slowing global growth.

A key feature of this record bull market is the persistent outperformance of Growth over Value. By almost any measure, Growth is trading at a historic valuation premium to Value and fund flows into Growth and Technology funds are at extreme levels. Value is trading at its largest discount to the market and offers the largest premium over the last 30 years. The median P/E of the cheapest portfolio relative to the S&P 500 is trading at a 7x discount (99% percentile) (JPM, The Value Conundrum, 6/7/19). Flows into the SPDR Technology ETF reached 95% percentile levels by the end of Q2 (Strategas, Technical Strategy, 6/26/19).

Figure 4: Forward Price/Earnings Spread – Value vs. Market

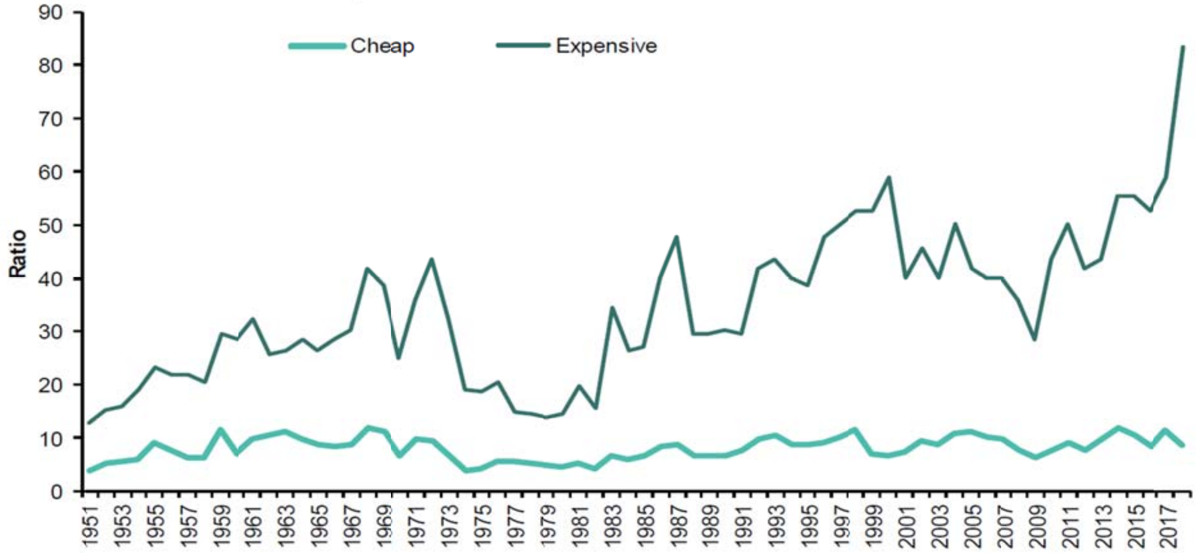


Source: JP Morgan, The Value Conundrum, 6/7/2019. Past performance is no guarantee of future results.

The considerable outperformance of Growth over Value has been attributed to the indexation and saturation of passive products which are pro-momentum, the perception that disruptive technologies have impaired wide swaths of companies in the Value space, and unconventional monetary policy (negative interest rates, quantitative easing). A number of events could trigger a reversal, including a market decline resulting in the liquidation of passive vehicles, increasing technology regulation or a reversal of the extreme crowding in Growth stocks.

With multiple expansion the major contributor to returns this market cycle, the underperformance of Value can partially be attributed to the greater benefit Growth has experienced from multiple expansion. Valuation dispersion within the S&P 500 is at cycle highs, marking a significant hurdle for future returns on the most richly valued part of the market.

Figure 5: Trailing P/E of the S&P 500's Highest and Lowest Quintiles



The lines show the market cap weighted trailing PE ratio of the most expensive and cheapest quintiles of the US market.
Source: Bernstein Research, Global Quantitative Strategy, 6/19/2019. Data as of the end of 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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