DISCIPLINED EQUITY

LARGECAP

GREAT LAKES ADVISORS

A WINTRUST WEALTH MANAGEMENT COMPANY

MANAGER COMMENTARY

Fourth Quarter 2018

Jon Quigley, CFA
Chief Investment Officer
Disciplined Equities

John D. Bright, CFA
Senior Portfolio Manager
Disciplined Equities

Dmitri Prokhorov
Research Analyst

Lyn Taylor
Research Analyst

Deepesh Bhatia
Research Analyst

MARKET REVIEW

U.S. equities suffered through a very poor fourth quarter, despite a good underlying economy and continued strong profitability. The relatively high valuation with which we entered Q4 combined with the Fed's measured rate normalization and slow runoff of the Treasury's massively expanded balance sheet are key drivers of the increased volatility of late.

Size/Style

In addition to the overall decline in stock prices, we also saw a reversal of style-based performance during the fourth quarter:

- Mega-caps performed in-line with large-caps.
- Valued outperformed growth stocks, especially in the mega-cap segment.

S&P 500 Sectors

We again saw a lack of quarter-to-quarter correlation of relative sector performance:

- Higher-yielding, counter-cyclical issues paced the market during the pullback. The Utilities and Real Estate sectors were the top two performers, with Consumer Staples and Health Care sectors following suit. The Health Care sector was the best performing S&P 500 sector for the calendar year.
- Energy stocks repeated their poor showing from the prior quarter, and had the largest decline of any sector for the year. The Tech sector declined over 17%, erasing all gains from the first nine months.

FOURTH QUARTER ATTRIBUTION

The LargeCap strategy declined about 13.7% during the quarter, just behind the benchmark S&P 500 Index's loss of 13.5%. The table below breaks down the contributions from sector positioning and stock selection.

In total, sector positioning detracted 0.35% from active return:

- Underweighting the Utilities sector detracted 42bps from active return, as the sector outperformed the S&P 500 Index by almost 15% during Q4.
- Underweighting the Energy sector added 36bps, as the sector underperformed the Index by about 10%.

Stock selection within the respective sectors added 0.16% to active return.

MARKET OUTLOOK

Any change from what we called the "pretty Goldilocks" condition of Q3 2018 could only be in one direction – and it was. But conditions are still pretty darned good.

Last quarter, we noted corporate profits had eclipsed their previous record; they did so again in the latest reported quarter, with margins still sitting north of 10%.

We also noted price pressures remained in check; since that writing, oil prices have slid into a bear market, pulling headline CPI back closer to 2% per year.

Employment numbers are also very strong. In addition to very low headline unemployment, we have workers re-entering the labor force (as evidenced by the simultaneous increase in the U-6 unemployment rate). And with a near-term supply-demand imbalance, employment costs continue to rise – meaning more than just shareholders are beginning to share in the fruits of this long expansion. And that has people – consumers and producers – feeling confident. But not as confident as they felt a month or two ago...

Washington, D.C. is right in the bullseye if we're looking for the cause of the withering confidence, lack of visibility, and increased volatility.

The mid-term elections held few surprises, but investors collectively wonder what the Democratic resurgence

“Any change from what we called the “pretty Goldilocks” condition of Q3 2018 could only be in one direction – and it was. But conditions are still pretty darned good.”

SECTOR	GLA WEIGHTING	S&P 500 WEIGHTING	% ACTIVE	GLA RETURN	S&P 500 RETURN	% ADDED	SECTOR ALLOCATION	STOCK SELECTION	ACTIVE CONTRIB
Comm Services	6.13%	9.97%	-3.85%	-17.30%	-13.19%	-4.11%	0.00%	-0.27%	-0.27%
Consumer Disc.	10.16%	9.91%	0.25%	-16.99%	-16.42%	-0.57%	-0.02%	-0.03%	-0.06%
Cons. Staples	6.95%	7.29%	-0.34%	-11.78%	-5.21%	-6.57%	-0.13%	-0.44%	-0.58%
Energy	2.48%	5.69%	-3.20%	-36.33%	-23.78%	-12.55%	0.36%	-0.40%	-0.04%
Financials	10.85%	13.49%	-2.64%	-9.86%	-13.10%	3.24%	0.04%	0.30%	0.34%
Health Care	21.81%	15.32%	6.48%	-6.19%	-8.72%	2.53%	0.28%	0.52%	0.80%
Industrials	14.47%	9.42%	5.05%	-14.86%	-17.25%	2.39%	-0.19%	0.36%	0.17%
Technology	24.05%	20.35%	3.70%	-17.91%	-17.34%	-0.58%	-0.17%	-0.14%	-0.31%
Materials	0.46%	2.56%	-2.10%	-6.22%	-12.31%	6.09%	-0.08%	0.07%	-0.01%
Real Estate	2.65%	2.85%	-0.20%	5.21%	-3.83%	9.04%	-0.02%	0.20%	0.18%
Utilities	0.00%	3.15%	-3.15%	0.00%	1.36%	-1.36%	-0.42%	0.00%	-0.42%
TOTAL	100.01%	100.00%	0.00%	-13.71%	-13.52%	-0.19%	-0.35%	0.16%	-0.19%

Source: GLA and Bloomberg. Performance numbers are gross of fees.

will mean – both in terms of policy, and in terms of the Presidency. We seem to have withstood the known unknowns of the Trump Presidency, but fret over the political unknowns which lie ahead.

To this political uncertainty, we add the usual rate hiking cycle of the Federal Reserve Board late in an economic expansion. All cycles are unique, and the Fed typically does not execute perfectly in attempting to allow a moderate expansion with little price pressure. This cycle is unique in at least two ways: The Fed is raising rates from a very low level, and it's embarked on the hikes with little sign of above-target inflation.

More impactful: The Fed is raising rates as the Treasury allows its massively-expanded balance sheet to runoff. This combination is as unprecedented as Trump and Pelosi's televised tête-à-tête… Americans like good reality TV, but markets generally don't like unprecedented combinations.

With all of this said, U.S. equities do appear attractive on a number of measures. Companies are generating high returns on assets/equity, are maintaining high margins, and now trade at a discount to historic valuation measures.

The LargeCap model remains biased against value stocks – especially the smaller value stocks in the LargeCap universe. The model is also biased against higher volatility stocks. Technology (Software) and Consumer Staples (Restaurants) stocks are most in favor, while Financials (Banks, Asset Managers) are most out-of-favor. Of note, Equity REITs have swung back into favor within the Financial sector, as higher dividend payers performed relatively well as Treasury yields dropped.

For more information, please contact us at:
marketing@greatlakesadvisors.com or 312-553-3700

The data in the attribution table represent the returns for each sector and for the gross returns for a representative composite account for one quarter ending the current calendar quarter. Individual account returns may vary.

Great Lakes Advisors, LLC ("Great Lakes" or "GLA") is an investment advisor registered with the Securities and Exchange Commission under the Investment Advisors Act of 1940. Established in 1981, Great Lakes is a subsidiary of Wintrust Financial Corporation and a part of the Wintrust Wealth Management family of companies. On October 1, 2013, majority owned subsidiary Advanced Investment Partners, LLC ("AIP") became fully-owned and integrated into Great Lakes. Great Lakes is a distinct business unit with distinct investment processes and procedures relating to the management and/or trading of investment portfolios for its clients.

Great Lakes Advisors, LLC claims compliance with the Global Investment Performance Standards (GIPS®). A complete list of firm composites and performance results, and the policies for valuing portfolios, calculating performance, and preparing GIPS compliant presentations are available upon request. Great Lakes Advisors, LLC's fees are available upon request and may be found in our Form ADV Part 2A. Performance data quoted herein represents past performance. Past performance does not guarantee or indicate future results. Returns and net asset value will fluctuate.

Manager commentary represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice. To determine if this strategy is appropriate for you, carefully consider the investment objectives, risk factors, and expenses before investing. The holdings, industry sectors, and asset allocation are presented to illustrate examples of the securities bought and the diversity of areas in which we may invest, and may not be representative of current or future investments. Portfolio holdings subject to change and should not be considered investment advice. The specific securities identified and described do not represent all of the securities purchased, sold or recommended for advisory clients and it should not be assumed that investments in the securities identified and discussed were or will be profitable. To obtain a list of all securities recommended during the past year, contact Great Lakes Advisors (GLA) at 312.553.3700. Actual clients' portfolios may or may not hold the same securities depending on the guidelines, restrictions and other factors of the specific portfolios.

Frank Russell Company ("FRC") is the source and owner of the Russell Index data contained or reflected in this material and all trademarks and copyrights related thereto. The presentation may contain confidential information and unauthorized use, disclosure, copying, dissemination, or redistribution is strictly prohibited. This is a GLA presentation of the Russell Index data. Frank Russell Company is not responsible for the formatting or configuration of this material or for any inaccuracy in GLA's presentation thereof.

Standard and Poor's, a division of the McGraw-Hill Companies, Inc., is the owner of the trademarks and copyrights relating to the S&P Index. The product is not sponsored, endorsed, sold or promoted by Standard and Poor's. Standard and Poor's makes no representation regarding the advisability of investing in the Product.

The index performance figures are calculated in U.S. dollars and reported on a gross basis. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Fees, including but not limited to the advisory fee, transaction and custody charges, would reduce the return. Investors cannot invest directly in an index. These indexes are not managed or sold by Great Lakes Advisors. Past performance is not indicative of future results. 19-6-0006.