Eagle Insight

EAGLE Asset Management
AN AFFILIATE OF CARILLON TOWER ADVISERS

Mid Cap Growth

Second Quarter | 2019

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Market Overview[1]

Mid-cap stocks continued their upward trajectory as the Russell Midcap® Growth Index (up 5.4%) and the Russell Midcap® Value Index (up 3.2%) both posted modest gains in the second quarter following very strong results in the first quarter. Returns were broadly positive across the Russell Midcap Growth Index, led by financials (up 10.5%), communication services (up 7.7%) and consumer discretionary (up 6.5%). Energy (down 4.5%) was the only sector posting negative returns during the quarter, while despite posting positive absolute returns, consumer staples (up 2.6%) also trailed the broader benchmark on a relative basis.

Portfolio Review[2,3]

The Eagle Mid Cap Growth portfolios outperformed the benchmark Russell Midcap® Growth Index on a gross and net basis during the second quarter. The portfolios' holdings within information technology most notably contributed to outperformance, while, to a lesser extent, solid absolute and relative returns within healthcare and financials also contributed to the portfolios' relative results during the quarter. A small amount of underperformance was experienced within consumer discretionary, which slightly weighed on the portfolios' broader outperformance in the period.

Shopify provides a cloud-based e-commerce platform that businesses can use to run their entire operations. The platform solution has been well received by the firm's very large addressable market, evident in the strong performance of shares during the quarter.

MarketAxess Holdings operates as an electronic trading platform focused on fixed-income investment instruments. The firm benefitted from healthy trading volumes – aided in part by a volatile interest rate environment – in addition to demonstrating meaningful market share gains that combined to drive shares higher.

Tableau Software, which sells business-intelligence analytics software, saw shares jump at the announcement that the firm was to be acquired by Salesforce.com at a substantial premium.

Caesars Entertainment, an iconic casino operator with a substantial presence in the all-important Las Vegas market, also saw shares rise after the announcement that it would be acquired by Eldorado Resorts at a sizable premium during the quarter.

Exact Sciences designs and develops molecular diagnostic tests used in cancer screening. Shares performed well as the firm has continued to benefit from robust insurance coverage (e.g., United Healthcare and Aetna) for its Cologuard exam product. In addition, increased physician adoption and an effective direct-to-consumer campaign are combining to help drive sales growth.

Qurate Retail operates TV retailers QVC and HSN, as well as online retailer Zulily. The firm continues to grapple with a perpetually evolving retail environment, as softer than expected results during the quarter led shares lower. We are encouraged by recent sizable insider purchases by management, and remain cautiously optimistic on Qurate and continue to hold the stock.

Canada Goose Holdings, which sells high-end outerwear, saw shares decline as the firm reported quarterly revenues above its own guidance range, yet failed to meet lofty Wall Street projections resulting in a reset of investor expectations. We remain constructive on the name as the firm continues to leverage the strength of its uniquely positioned brand to drive industry-leading growth.

Lions Gate Entertainment shares waned in light of the firm's mixed results reported during the quarter. However, recent success with its latest movie release, "John Wick 3," is poised to boost Lions Gate in the near-term. The firm is also pursuing a partner to assist with robust international expansion plans for its Starz segment, providing growth prospects moving forward.

Bluebird bio, a biotechnology firm engaged in developing immunotherapy-focused treatments for cancer indications, saw shares decline as competitive concerns persisted from industry peer Amgen in the multiple myeloma cancer space. Bluebird is expected to publish phase-3 results for its own drug candidate in the back half of 2019. We believe the results should help to dispel the perceived competitive concerns.

Intuitive Surgical manufactures robotic surgical systems. The firm shares decline modestly as it shifted focus from its traditional sales model towards a more consistent (but comparatively smaller) revenue stream via the offering of operating leases for its DaVinci systems. This seemed to give investors pause as they wrestled with the resulting effects on Intuitive's forward growth prospects.

Outlook[2]

Equity markets extended the strong performance of the first quarter, benefitting from a strong domestic economy as well as a presumably dovish Federal Reserve (Fed). Markets currently seem to be reacting to the bond market with particular interest in how it forecasts pending actions by the Fed. As of this writing, the bond market is forecasting a 50 basis point cut in interest rates at the Fed meeting in late July. However, the Fed may be in a bind: At its last meeting, it said it would act as appropriate to sustain economic growth, which the markets interpreted as meaning a rate cut is pending. However, recent domestic economic data has been positive, with the jobs number being particularly strong. President Trump's constant criticism of the Fed also seems to be further muddying the water. Needless to say, it will be an interesting meeting.

In the third quarter, equity markets generally shift their attention to the following year – or in this case, 2020 – which is an election year. Given the strength of the recent rally, generally slowing global growth, which continues to be impacted by tariff disputes, difficult earnings comparisons ahead and relatively expensive valuations, we would not be surprised by some volatility in the months ahead.

During the first six months of 2019, the energy sector has been one of the worst-performing sectors. Oil price volatility remains high as markets grapple with concerns over relentless supply growth in North America and weakening global economic data. Despite these concerns, our balanced view on the downtrodden sector is based on likely continued central bank easing and a possible extension of OPEC+ self-imposed production cuts. Equity market investors continue to favor the select few exploration and production (E&P) operators that are capable of generating free cash flow and growing production. Given current commodity prices, we believe that this "dual mandate" will continue to prove to be a challenging feat for an industry that is notorious for generating returns below its cost of capital. As such, we expect operators with access to the most economic resource base will continue to outperform, and we remain positioned accordingly.

The outlook for the industrials and materials sectors remains heavily contingent on two fac-

Top 10 Holdings

Waste Connections
SBA Communications Class A
ServiceNow
Keysight Technologies
TransUnion
Lululemon Athletica
MarketAxess Holdings
Martin Marietta Materials
Monster Beverage
IHS Markit

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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Mid Cap Growth

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	Top Securities	Average Weight (%)	Security Contribution to Portfolio Return	Bottom Securities	Average Weight (%)	Security Contribution to Portfolio Return
Mid Cap Growth	Shopify	1.18	0.47	Qurate Retail	0.80	-0.26
	MarketAxess Holdings	1.62	0.45	Canada Goose Holdings	0.75	-0.18
	Tableau Software	1.01	0.38	Lions Gate Entertainment	0.58	-0.14
	Caesars Entertainment	0.71	0.35	bluebird bio	0.54	-0.13
	Exact Sciences	1.00	0.33	Intuitive Surgical	0.55	-0.11

*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.

Investments in mid-cap companies generally involve greater risks than investing in larger capitalization companies. These companies often have narrower commercial markets and more limited managerial and financial resources than larger, more established companies. As a result, their performance can be more volatile and they face greater risk of business failure, which could increase the volatility of a fund's portfolio. Additionally, small-cap companies may have less market liquidity than larger companies.

Growth companies are expected to increase their earnings at a certain rate. When these expectations are not met, investors may punish the stocks excessively, even if earnings showed an absolute increase. Growth company stocks also typically lack the dividend yield that can cushion stock prices in market downturns. The companies engaged in the technology industry are subject to fierce competition and their products and services may be subject to rapid obsolescence. The values of these companies tend to fluctuate sharply.

tors which are well known to investors. First, these cyclically sensitive areas of the stock market will continue to vacillate on investors' perceptions of progress – or lack thereof – in the ongoing trade negotiations between China and the United States. The timing of a final trade resolution – and whether one can be reached at all – will undoubtedly continue to be the primary uncertainty in the minds of investors. Perhaps more importantly, it will be top of mind for corporate executives across the globe who are making capital investment decisions.

The second factor that may determine the performance of the industrial and materials sectors will be the future path of the Fed's monetary policy. Indeed, both sectors have already benefitted year-to-date from the so-called "Powell pivot." The Fed chairman abruptly transitioned in a few short months from a policy hawk who bravely proclaimed that the fed funds rate was "a long way from neutral" to a dove terrified by future implications of an inverted yield curve. Further gains in the back of 2019 appear possible if the Fed can demonstrate its commitment to move towards easier monetary policy in the face of subdued inflationary data. We currently believe that a rate cut from the Federal Reserve will likely lead to a steepening of the yield curve and push investors into the more cyclically sensitive sectors of the market, which offer attractive valuations – especially relative to "growthier" areas of the market where multiples have expanded considerably.

In our view, the environment within healthcare remains poised to support greater-than-GDP growth rates given the combined tailwinds of an aging population, longer lifespans, the crippling impact of chronic conditions and new medical innovations. The adoption of high-deductible health plans, coupled with health savings accounts (HSAs), has forced employees to shoulder a much larger burden of their insurance premiums and other out-of-pocket healthcare expenses, ultimately encouraging patients to more closely scrutinize their care-related decisions. We also believe that consolidation through mergers & acquisitions (M&A) activity is likely to continue throughout the healthcare industry.

We strive to identify healthcare companies that offer disruptive technologies or services that will drive significant revenue growth for these companies for years to come. One example of this is the disruptive nature of telemedicine: This care innovation continues to see rapid adoption by managed care and health care systems, particularly due to the convenience of improved access to quality care at a lower cost compared to in-person primary care office visits. In addition, we continue to like companies that provide "cash-pay" products and services (e.g., aesthetics, veterinary products and services, as well as dental and orthodontic procedures) which tend to have little regulatory or reimbursement risk from the federal government. Finally, we continue to seek opportunities within the biotechnology industry, where many firms are developing revolutionary therapies to treat diseases and conditions that would have otherwise been chronic, expensive, or fatal.

The outlook for the financials sector remains mixed. Moderating economic growth, lower levels of interest rates and a flatter-to-inverted yield curve make for challenging fundamentals in the core banking space. Outside of core banking, we are seeing unique opportunities in the insurance space in the form of companies created post-Great Recession to underwrite private mortgage insurance. In addition, although the first half of 2019 was relatively modest from an M&A perspective, we expect that pace to accelerate through the balance of the year. We continue to favor smaller boutique M&A advisor opportunities which have been gaining market share from the larger firms. Additionally, we remain constructive on select U.S. consumer pawn operators who are exporting their business model to the faster growing and more fragmented markets of Latin America.

We remain optimistic regarding information technology-related spending as unemployment rates remain at multi-decade lows, and consumer confidence and small business optimism indicators remain healthy. With interest rates pulling back, technology spending should remain robust both at the enterprise and consumer levels. M&A activity within information technology has remained healthy and we would expect that, with strong balance sheets at the very large technology companies and a sympathetic political environment in Washington, real potential exists for that trend to continue. We remain focused on high-quality companies with strong management teams that are well-positioned to gain market share. Additionally, we are looking for names that benefit from long-term secular growth trends with themes that include cloud computing, artificial intelligence, mobility, e-commerce/digital payments, Internet of Things/smart home, factory/industrial automation, security software, e-gaming and alternative energy.

Within the consumer sector the key theme is focus on the Millennial demographic. Millennials spend more on experiences over goods. They prefer the flexibility of renting housing rather than purchasing a home. They buy predominately online and are heavily influenced by social media, particularly social media influencers. They prefer their meals delivered and eat fake meat. They spend heavily on their pets. These preferences are in sharp contrast to prior generations, and the changes have created both winners and losers within the consumer space. Companies that are doing well are able to address the needs of Millennials by merging social media with online retail and addressing these rapidly changing preferences.

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3. Source: FactSet, Frank Russell Co. Statistics represent an aggregate of all Mid Cap Growth portfolios.