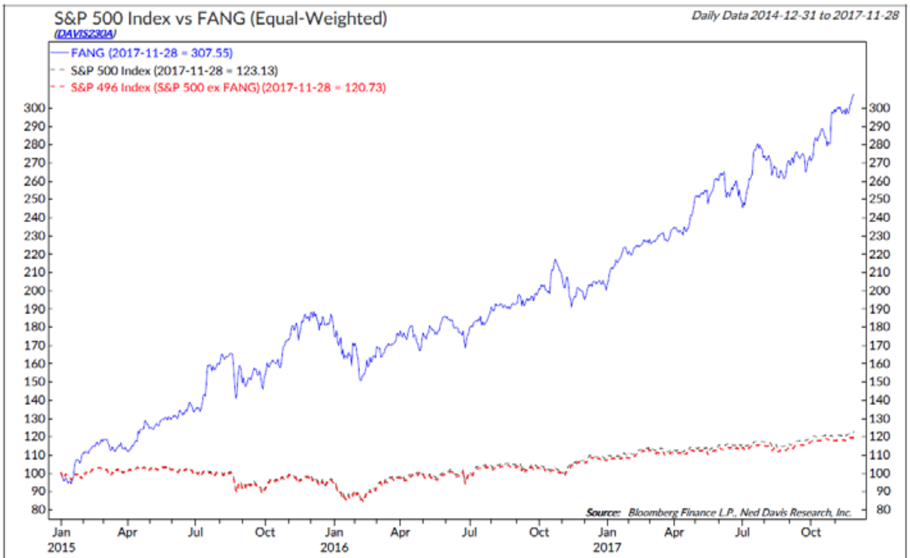
December 1, 2017

"The individual investor should act consistently as an investor and not as a speculator."
-Benjamin Graham, Warren Buffett's mentor



Ticker	Name
FB	Facebook
AMZN	Amazon.com
NFLX	Netflix
GOOGL	Alphabet

Index (Equal-Weighted)	Gain/Annum % 2014-12-31 to 2017-11-28	YTD % 2016-12-30 to 2017-11-28
FANG	47.07	53.70
S&P 500 Index	7.40	14.14
S&P 496 Index (S&P 500 ex FANG)	6.68	13.18

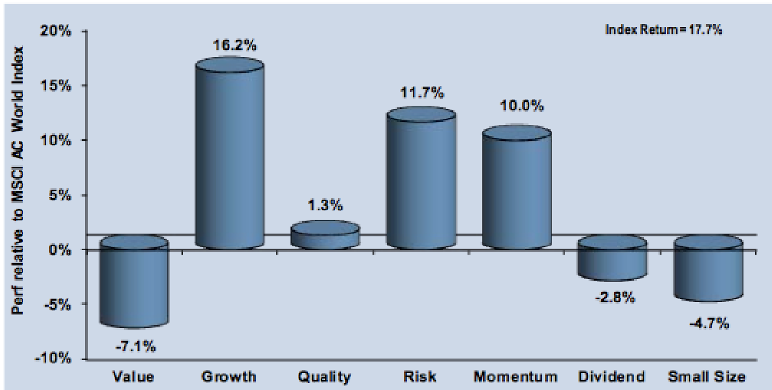
Source: Ned Davis Research

One of the most pervasive themes in global equity markets in 2017 has been investors' insatiable appetite for growth – no matter the price. The leader of our investment team, George Shipp, has said investors should not divide the investing world between growth or value, we want to invest in both. Thankfully as we come toward the end of the year we have a number of stocks in the portfolios that have attractive growth and value characteristics. What has been remarkable this year is the willingness of the market to pour money into stocks with meaningful revenue growth regardless of valuation and a corresponding disdain for value. Perhaps nowhere is this dynamic represented better than in the performance of the infamous FANG stocks (Facebook, Amazon, Netflix, and Google). In 2017, FANG stocks equally weighted are up roughly four times the S&P 500. Market strategists have attributed the reason for their exceptional performance due to their secular growth stories that should play out with a high degree of certainty.

FANG has led the performance of growth stocks in 2017 with the Russell 1000 Growth up 28% as of the end of November versus the 12% increase in the Russell 1000 Value. Another view of the quest for growth regardless of price can be found in the performance of the top 10% of growth stocks in various benchmarks. In the S&P 500, for example, the top 10% of stocks ranked by sales growth over the past year are up 27% year-to-date, or 35% above the performance of the index according to Bloomberg. But these stocks are trading at valuations roughly twice that of the index on a price-to-earnings ratio. Globally the same dynamic can be witnessed. In the Bloomberg World Index using the same criteria, the top 10% of growers were up 65% more than the index and are trading at roughly a 50% premium on an earnings basis. Clearly, investors are paying less attention to valuation and more for growth dynamics.

Going back to FANG and what has driven price appreciation this year, we can break down the roughly 50% equally weighted total return for the four stocks between valuation expansion and earnings growth. Since the beginning of the year FANG's price to earnings multiple has expanded almost 30% from 35x to 45x forecasted earnings. In the meantime, earnings for the first nine months of 2017 are up 22%, so the majority of price appreciation is driven not by earnings but investors placing a higher value on those earnings.

Chart 3: Quantessential Style relative performance: YTD



Source: BofA Merrill Lynch Global Quantitative Strategy, MSCI, IBES, S&P, Worldscope, Bloomberg
Performance is based on our monthly-rebalanced 30-stock Quantessential Styles.

Lower valuations have typically helped stock prices outperform, but not this year. Ned Davis Research notes that over the past 33 years, the simple valuation measure of stocks that are cheap on price relative to their revenues would typically outperform by 3.6% per year, but this year that characteristic has resulted in (13%) underperformance. Likewise Merrill Lynch's domestic and global strategists note that a value bias in the general market has not helped performance in 2017. In the S&P 500, for example, the cheapest 10% of the index has underperformed by 15% since October. Likewise, in the MSCI ACWI index, value has underperformed by 7.1% this year as seen in the chart above.

It's worthwhile to note that within FANG our portfolios own Google. What makes Google different within FANG is that Google generated the majority of FANG profits as of the end of September (57%). Google is also the cheapest of the FANG components and trades at a price to earnings multiple below its forecasted 2018 growth rate, a common indicator of value relative to growth. Our ownership of Google within FANG is indicative of our investment approach of looking for unique growth companies, but also with attractive valuation characteristics – we want both growth and value.

As always, we thank you for your interest and trust managing your investments.

Chip Wittmann, CFA®
Executive Director
(757) 417-4901
cwittmann@sterling-capital.com