TCW

MANAGED ACCOUNTS DIVISION

TCW Relative Value Large Cap

FOURTH QUARTER 2018 | INFOFLASH

Philosophy: A strategy seeking undervalued, large cap stocks where the company has a fundamental catalyst or competitive advantage which will ultimately be recognized by the market place and appreciate in value.

Key Issues

- The combination of tense trade negotiations between the U.S. and China, signs of slowing global economic growth, interest rate hike jitters, and the prospect of a protracted U.S. government shutdown triggered a dramatic sell-off in equities in the fourth quarter. Before being upended by the worst December since 1931, October's S&P 500 performance was the worst month in more than seven years accompanied by a rare simultaneous decline in bond prices. U.S. equities bounced back in November though the road was bumpy. While the same causes that led to the sharp decline in October (and again in December) still hovered, investors had reasons to be optimistic. Early in the quarter, the Bureau of Labor Statistics report showed robust jobs growth in October along with 3.1% (year-over-year) wage growth and the unemployment rate at 3.7%, close to a fifty-year low. Stocks then got a big boost upon the outcome of the midterm elections which resulted in the Democrats taking back control of the House of Representatives. Equities got a further lift after Britain and the European Union agreed on a Brexit deal, though Prime Minister Theresa May postponed her country's early December Parliamentary vote as indications suggested it would most likely be rejected. The markets rallied after Fed Chairman Jerome Powell's speech on November 28 to the Economics Club of New York. However, November's rosier outlook dissipated in December with fears of the Fed maintaining its independence, U.S. cabinet level/military disagreements, a partial U.S. government shutdown, and the looming March 1st U.S./China truce deadline.
- Over the course of the fourth quarter, the best performing sectors in the S&P 500 were utilities (+1.4%), real estate (-3.8%), and consumer staples (-5.2%), while the bottom performers were energy (-23.8%), information technology (-17.3%), and industrials (-17.2%). The portfolio benefited from the underweights in information technology and consumer discretionary while the overweights in energy and industrials and underweight in consumer staples detracted. Looking at security selection, the portfolio derived its best relative contribution from its consumer staples holdings, while the biggest negative occurred within the portfolio's industrials stocks.
- While any significant slide in stocks is unpleasant, it is worth noting that including this sell-off, there have only been six corrections (defined as a 10% decline) since the recent bull market began in March 2009. We believe investors should continue to expect volatility in the short term, as Washington works to end the partial government shutdown while trade negotiations between the U.S. and China continue, but are unlikely to be completed by the March 1st deadline. It has been noted by us and others that the U.S. yield curve has reached its flattest level since prior to the great recession of 2008/09. While an inverted curve has proven to be an effective harbinger for a recession, we believe none is imminent given the relative strength of the U.S. economy. Fundamentally at least, there has been a short-term shift from growth to value beginning in the fourth quarter. Year-to-date through September, the Russell 1000 Growth outperformed its Russell 1000 Value counterpart by over thirteen percent. However, for the calendar year, that margin has been nearly halved with the Value Index outperforming by over four percent in the fourth quarter. The Financial Times (December 5) reported that "Not dead yet - Value stocks show signs of resilience amid autumn turmoil." Within the article, Morgan Stanley is cited stating it believes there is a "major leadership change occurring from growth to value which could be more long-lasting than most appreciate." We agree.

Top Ten Holdings

AS OF DECEMBER 31, 2018

Name		% of Portfolio
1.	Cisco Systems Inc.	4.7
2.	JPMorgan Chase & Co.	4.5
3.	Merck & Co. Inc.	4.3
4.	Comcast Corp.	4.0
5.	Intercontinental Exchange Inc.	3.9
6.	Textron Inc.	3.6
7.	Citigroup Inc.	3.4
8.	Chevron Corp.	3.4
9.	Corning Inc.	3.4
10.	The Procter & Gamble Co.	3.1

Source: TCW. Based on a managed account model portfolio. Portfolio characteristics and holdings are subject to change at any time. It should not be assumed that an investment in the securities listed was, or will be, profitable.

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Representative Equity Buys and Sells

BUYS (Ticker; Sector)

International Business Machines Corp. (IBM; Information Technology)
IBM is an information technology provider whose offerings include IT infrastructure, software, and services for enterprises worldwide. Recently, the company has introduced new products in the areas of data analytics, security, and artificial intelligence. These new products are typically monetized via services or software revenue and we believe should lead to increasing growth rates in those businesses. IBM has repeatedly transformed its operations over time and over the past decade or so has divested almost $15 billion in annual revenue as they continually exit lower-value businesses in favor of higher-value new opportunities with the effect of pulling margins higher. We expect this restructuring trend to continue.

ConAgra Brands Inc. (CAG; Consumer Staples)
ConAgra Brands is a leading packaged food manufacturer. The company's CEO, Sean Connolly, has already implemented a significant positive transformation by upgrading CAG's brand portfolio through acquisitions and divestitures, bringing costs down, and increasing innovation. The company recently announced it would be purchasing Pinnacle Foods, a medium-sized food manufacturer for $8.1 billion. We believe the acquisition provides numerous means to enhance value including adding scale to CAG's already large frozen foods business and generating synergies.

Target Corp. (TGT; Consumer Discretionary)
Target is a general merchandise retailer. Target is modernizing its supply chain operations to become a leading omnichannel retailer. The company is remodeling stores and opening smaller format stores in urban and college campus locations; these new smaller format locations are proving to be twice as productive as current locations. Finally, Target is launching a dozen new private label brands in the higher margin home and apparel categories.

SELLS (Ticker; Sector)

Synchrony Financial (SYF; Financials)
Synchrony Financial is a consumer finance company specializing in private label credit cards and installment lending. Despite effectively executing by winning the PayPal portfolio, as well as successfully renewing longstanding relationships with J.C. Penney and Lowe's, we believe the loss of both Walmart and potential loss of Sam's Club would put a strain on Synchrony successfully delivering on its new markets/products catalyst.

ON Semiconductor Corp. (ON; Information Technology)
ON Semiconductor is a global provider of semiconductor devices. The primary catalyst was restructuring related to the significant expected synergies following a recent acquisition. In our view, the company has executed well on the integration work thus far, with further margin expansion expected. However, following a fundamental review, it was determined that ON's hefty automotive end market exposure and Asia-based supply chain "stress test" (in the event of an escalating trade war with China) would continue to pressure the stock.

The Goldman Sachs Group Inc. (GS; Financials)
At the center of its consumer lending initiative was Marcus, its online lending platform, but by October of 2018, management announced it would curtail growth as it became concerned about credit risk. Additionally, new revelations and reputational damage surrounding Goldman's involvement in the 1MDB scandal led to a fundamental review flag and likely limits its upside in the near term. Sitting in between strategic plans and saddled with a regulatory overhang, we concluded the downside risks outweigh the potential upside.

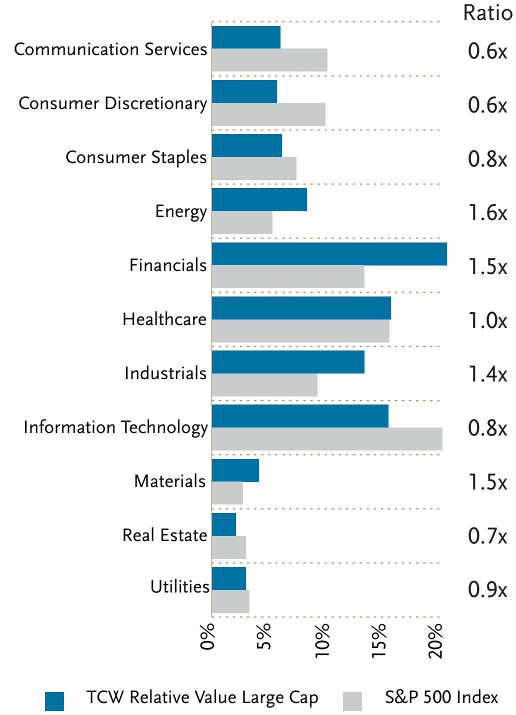
Portfolio Profile

AS OF DECEMBER 31, 2018

Equities	TCW	S&P 500 Index	Russell 1000® Value Index
Number of Securities	47	505	725
Price-to-Cash Flow	10.1x	13.5x	11.1x
Price-to-Sales	1.2x	2.2x	1.7x
Price-to-Earnings Ratio Avg.–Next 12 Months	10.9x	14.6x	12.6x
Price-to-Book	1.8x	3.1x	1.9x
Projected EPS Growth-F2 Year (annualized)	9.3%	9.6%	7.2%
Dividend Yield	2.6%	2.2%	2.9%
Market Capitalization			
Average ($ Wtd.)	$87.0 bil	$201.2 bil	$118.4 bil
Average (Eq. Wtd.)	$62.1 bil	$46.0 bil	$23.2 bil
Median	$23.9 bil	$18.5 bil	$8.3 bil

Sector Analysis

AS OF DECEMBER 31, 2018



Source: TCW

Note: Sector weights calculated as percent of equities.

Based on a managed account model portfolio. Portfolio characteristics and holdings are subject to change at any time. The investment strategy does not target any specific numbers or ranges for these characteristics. Accordingly, these characteristics can vary greatly. The estimates are forward-looking statements based on assumptions. This would include forward earnings estimates and growth rates, among other things, and all associated calculations, including projected price/earnings ratios. Actual results may vary materially from the estimates due to the numerous economic, financial and market conditions. There is no assurance that forecast estimates will be realized. The index is not available for direct investment; therefore its performance does not reflect a reduction for fees or expenses incurred in managing a portfolio. The securities in the index may be substantially different from those in the strategy.

Reflects up to the three largest buys (new buys) and up to the three largest sells (complete sells) for the quarter. There is no assurance that any securities discussed herein will remain in an account; be purchased in the portfolio at the time this report is received or that securities sold have not been repurchased. It should not be assumed that any of the securities transactions or holdings discussed were, or will prove to be, profitable or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein.

S&P 500: Widely regarded as the best single gauge of the U.S. equities market, this world-renowned index includes a representative sample of 500 leading companies in leading industries of the U.S. economy. Although the S&P 500 focuses on the large-cap segment of the market, with over 80% coverage of U.S. equities, it is also an ideal proxy for the total market.

Russell 1000® Value: The Russell 1000® Value Index is representative of the U.S. market for large capitalization stocks containing those companies in the Russell 1000® Index with lower price-to-book ratios and lower forecasted growth.

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