

Fourth Quarter 2017



BRIAN E. GRANEY, CFA
Portfolio Manager

COMPOSITE PERFORMANCE (%)

	COMPOSITE GROSS OF FEES	COMPOSITE NET OF FEES	S&P 500® INDEX
3 MOS.	6.80	6.66	6.64
1 YR.	21.45	20.78	21.83
3 YR.	8.66	8.05	11.41
5 YR.	13.04	12.39	15.79
ITD (01/10/2010)	13.31	12.66	14.86

The composite performance shown above reflects the Brown Advisory Equity Income Composite, managed by Brown Advisory Institutional. Brown Advisory Institutional is a division of Brown Advisory LLC, and Brown Advisory Institutional is a GIPS compliant firm. Please see the end of this for a GIPS compliant presentation.

REP. ACCOUNT CHARACTERISTICS

	EQUITY INCOME REP. ACCT.	S&P 500 INDEX
Weighted Avg. Market Cap.	\$178.2 B	\$196.7 B
P/E Ratio (FY2 Est.)	19.1x	18.1x
Active Share	77.7%	
Dividend Yield	2.5%	1.8%
Portfolio Beta (Since Inception)	0.76	
Return on Equity (ROE)	19.6%	19.3%
Portfolio Turnover (3 Yr. Avg.)	11.6%	--

REP ACCOUNT. TOP 10 PORTFOLIO HOLDINGS

SECURITY	% PORTFOLIO
Microsoft Corp.	4.9
Altria Group, Inc.	4.8
Cash & Equivalents	4.6
Apple, Inc.	3.9
McDonald's Corp.	3.5
AbbVie, Inc.	3.5
JPMorgan Chase & Co.	3.3
Philip Morris International, Inc.	3.3
Cisco Systems, Inc.	3.3
Automatic Data Processing, Inc.	3.0
TOTAL	38.1

Review & Outlook

U.S. stocks rose in the fourth quarter, extending gains for investors that were generated fairly consistently and evenly throughout all of 2017. The fuel tank for the stock market's steady rise for the quarter and the year was a backdrop of synchronized global economic growth that, in turn, helped generate healthy corporate profits worldwide. The strategy rose in line with its benchmark, the S&P 500® Index, for the quarter and trailed slightly for the full year.

The information technology (IT) sector was far and away the best sector for investors during the year. Fast-growing (but non-dividend paying) companies, such as Amazon.com and Facebook, garnered significant investor attention, and their stock prices surged over 50% for the year. Yet, IT was not the only area of the market that generated sizable gains. On a sector basis, six of the eleven sectors in the benchmark saw gains of 20% or more in 2017. Likewise, the strategy saw notable gains from a variety of stocks during the year, with 17 existing holdings rising in price by more than 25% and nine holdings rising by more than 40%. In sum, it was a good year to be a diversified investor with broad exposure to different parts of the market.

The strategy's industrial holdings struggled and detracted from overall performance during the fourth quarter and the full year. In particular, industrial conglomerate **General Electric's** stock declined considerably during the quarter after the company reported earnings that were far below expectations and projected continued weakness in its power and oil and gas businesses. Clearly, we made a mistake in over-estimating the near-term earnings power of the company. But it was a lack of confidence in projecting GE's long-term earnings power that led to our decision to exit the stock during the quarter.

The situation was much more favorable for the strategy's consumer discretionary holdings during the quarter and for the full year, as that sector was a significant contributor to performance. In fact, all of the strategy's holdings in the sector rose in price during the fourth quarter except for a new intra-quarter addition, **Hasbro Inc.** Hasbro is a high-quality toy and entertainment company with valuable brands and global manufacturing and distribution scale. The outlook for future earnings and dividend growth is bright, as the company's management team has demonstrated a capability to monetize its core brand platforms beyond just toys and into areas such as film, TV, digital streaming, social media and gaming.

An additional bright spot for the strategy during the fourth quarter was the IT sector, where holdings such as **Microsoft** and **Cisco Systems** continued to gain business momentum. Businesses worldwide are investing more resources into their IT systems. As a result, revenue growth is accelerating and margins are expanding at leading IT vendors, such as Microsoft and Cisco. Elsewhere within the IT sector, chipmaker **Qualcomm** jumped in price after receiving an unsolicited takeover offer from fellow chipmaker Broadcom during the quarter. Due to the unclear timing and uncertain regulatory hurdles of the proposed combination, we reduced our position in Qualcomm after the acquisition bid announcement.

The strategy also added medical devices firm **Medtronic** to the portfolio during the quarter. Hurricane Maria caused disruptions to the company's Puerto Rico manufacturing operations, which created a favorable entry price into the stock. Longer term, we expect Medtronic, with its product and geographical scale, will generate the type of steady, predictable earnings and dividend growth that we value in all of our investments. It joins a list of existing companies in the portfolio that, in aggregate, offer above-average dividend yields with a strong potential for future growth at a reasonable level of valuation. [B](#)

Sector Diversification

- Our weighting in consumer discretionary rose during the quarter as we added Hasbro to the portfolio. The strategy is currently overweight in the consumer discretionary sector after having been underweight previously.
- Our weighting in industrials fell during the quarter as we eliminated General Electric from the portfolio. The strategy is currently underweight in the industrials sector after having been overweight previously.
- Our health care weighting increased during the quarter as we added Medtronic to the portfolio. Despite this addition, the strategy remains underweight in the health care sector.
- We have no exposure to the telecommunication services and utilities sectors because of what we consider to be unattractive valuations and limited potential for dividend growth rates in both sectors.

SECTOR	EQUITY INCOME REP. ACCOUNT (%)	S&P 500 ® INDEX (%)	DIFFERENCE (%)	EQUITY INCOME REP. ACCOUNT (%)	
	Q4 '17	Q4 '17	Q4 '17	Q3 '17	Q4 '16
Consumer Discretionary	12.27	12.14	0.13	10.16	11.34
Consumer Staples	13.78	8.20	5.58	14.49	14.23
Energy	5.21	6.07	-0.86	5.04	4.70
Financials	17.67	14.78	2.88	17.59	18.24
Health Care	12.61	13.84	-1.23	11.79	11.75
Industrials	9.35	10.26	-0.91	12.22	13.27
Information Technology	20.24	23.83	-3.59	19.84	19.42
Materials	2.03	3.00	-0.96	1.97	1.19
Real Estate	6.85	2.89	3.96	6.90	5.86
Telecommunication Services	--	2.06	-2.06	--	--
Utilities	--	2.93	-2.93	--	--

Quarterly Attribution Detail by Sector

- The industrials sector was the biggest detractor from performance during the quarter due to unfavorable stock selection. Of the strategy's five holdings in the sector, four declined in price during the period.
- Information technology and consumer discretionary were the largest contributors to comparative performance because of favorable stock selection in both sectors. Consumer discretionary was the best performer within the benchmark during the quarter.
- The strategy's lack of exposure to the utilities sector contributed to comparative performance. The utilities sector was the weakest performer within the benchmark during the fourth quarter.

SECTOR	EQUITY INCOME REP. ACCOUNT		S&P 500 INDEX		ATTRIBUTION ANALYSIS		
	AVERAGE WEIGHT (%)	RETURN (%)	AVERAGE WEIGHT (%)	RETURN (%)	ALLOCATION EFFECT (%)	SELECTION AND INTERACTION EFFECT (%)	TOTAL EFFECT (%)
Consumer Discretionary	11.27	13.86	11.91	10.08	0.01	0.38	0.39
Consumer Staples	13.99	3.03	8.11	6.49	-0.03	-0.47	-0.50
Energy	5.00	7.18	5.93	6.02	0.02	0.06	0.08
Financials	17.53	8.52	14.66	8.63	0.06	-0.02	0.04
Health Care	12.71	2.16	14.16	1.47	0.08	0.09	0.17
Industrials	10.21	-2.80	10.15	6.09	-0.03	-0.98	-1.01
Information Technology	20.24	13.96	24.02	8.91	-0.07	0.94	0.87
Materials	2.01	11.27	2.99	6.93	--	0.09	0.08
Real Estate	7.04	4.25	2.96	3.22	-0.13	0.07	-0.06
Telecommunication Services	--	--	1.97	3.54	0.07	--	0.07
Utilities	--	--	3.12	0.21	0.19	--	0.19
Total	100.00	6.97	100.00	6.65	0.16	0.16	0.33

Quarterly Contribution to Return

- Software maker Microsoft gained after reporting strong quarterly results that featured better-than-expected revenues and margins from its fast-growing commercial cloud services business. The company also raised its margin target for the coming year.
- Tobacco company **Altria** rebounded from a weak third quarter, when the stock declined after the FDA announced that it is considering placing limits on the amount of nicotine allowed in traditional cigarettes. In the fourth quarter, Altria reported earnings that were above expectations and hosted an investor day that highlighted a number of new tobacco products for the U.S. market. Drug maker AbbVie rose after reporting strong first quarter growth of its key drug, Humira, in the U.S. Additionally, recent clinical trial results from AbbVie's pipeline drugs in immunology have been favorable, supporting the long-term growth opportunity for the company.
- Chipmaker Qualcomm rose after rival semiconductor maker Broadcom announced an unsolicited takeover offer for the company. We reduced our position size after the announcement, based on the uncertain timing of the proposed combination. Subsequently, Qualcomm's board rejected the takeover offer on the basis that the proposal "significantly undervalues" the company. **Altria** rose during the quarter after reporting solid first quarter earnings. Sales of the company's tobacco products in the U.S. are holding up relatively better than other consumer products, where sales have been generally sluggish. Also, there was increased speculation during the quarter that Altria could potentially reunite with **Philip Morris International** at some point through a merger.
- Networking company Cisco Systems gained after reporting better-than-expected quarterly earnings. The company forecasted accelerating revenue growth in the coming quarters due to successful new product launches and higher customer adoption of subscription-based services.
- Apparel maker **V.F. Corp** rose after reporting better-than-expected quarterly sales and earnings. The company also raised its dividend by 10% and announced a small acquisition of specialized outdoor apparel brand: Icebreaker Holdings.
- Industrial conglomerate General Electric fell after reporting quarterly earnings that were well below expectations. In particular, the company struggled to generate significant cash flow from its power and oil gas businesses in the quarter. The lower cash flow forecast prompted us to eliminate the stock after the earnings report and ahead of a potential dividend cut, which became a reality later in the quarter.
- **Merck** dropped after the drugmaker delayed filings and trials related to its important immuno-oncology drug, Keytruda. In the short term, competing drugs could gain ground on Keytruda, and the company's revenue growth in the coming year could be limited. But over the longer term, Keytruda's future as an effective therapy for different forms of cancer remains bright.

EQUITY INCOME REP. ACCOUNT TOP FIVE CONTRIBUTORS				
TICKER	NAME	AVG. WEIGHT (%)	RETURN (%)	CONTRIBUTION TO RETURN (%)
MSFT	Microsoft Corporation	5.07	15.42	0.75
MO	Altria Group, Inc.	4.81	13.62	0.63
QCOM	QUALCOMM Incorporated	2.02	24.52	0.53
CSCO	Cisco Systems, Inc.	3.30	14.87	0.48
VFC	V.F. Corporation	2.63	17.15	0.43
EQUITY INCOME REP. ACCOUNT BOTTOM FIVE CONTRIBUTORS				
GE	General Electric Company	0.65	-15.59	-0.33
MRK	Merck & Co., Inc.	2.15	-11.37	-0.29
NLSN	Nielsen Holdings Plc	2.20	-11.35	-0.29
PM	Philip Morris International Inc.	3.59	-3.85	-0.16
UN	Unilever NV ADR	3.07	-4.01	-0.13

- Data measurement company **Nielsen** fell after forecasting lower revenue growth and margins in the coming year. The company intends to increase investment spending and cut costs as it tries to rejuvenate stagnant growth in its business segment that caters to consumer packaged goods companies.
- Household products company **Unilever** and tobacco company **Philip Morris International** dropped because, as internationally based companies, neither firm will benefit from the tax reform that will result in a lower corporate tax rate for U.S.-based companies.

Portfolio Activity

- During the quarter, we added toymaker Hasbro, Inc. to the portfolio. Hasbro is a high-quality global play and entertainment company. Through its lineup of globally recognized brands, Hasbro is well-positioned for future earnings and dividend growth, in our view.
- We also added medical device maker Medtronic to the portfolio. Medtronic has a global presence in the medical technology market and distributes its products and services to hospitals, physicians and health care professionals in approximately 160 countries. We expect its earnings and dividend to increase at a stable and attractive rate over time.
- General Electric was one of the worst performers in the S&P 500 Index throughout 2017. In the fourth quarter, GE missed earnings expectations by a wide margin and slashed cash flow guidance for the remainder of the year. While we were hopeful that the company's new CEO could execute on a plan to turn the company around, we believed the company's financial condition posed a threat to the continuation of its current dividend. Given this, we exited our position in GE during the quarter.

EQUITY INCOME REP. ACCOUNT PORTFOLIO ACTIVITY		
ADDITIONS		SECTOR
HAS	Hasbro, Inc.	Consumer Discretionary
MDT	Medtronic plc	Health Care
DELETIONS		SECTOR
GE	General Electric Company	Industrials

Brown Advisory Equity Income Composite

Year	Composite Total Gross Returns (%)	Composite Total Net Returns (%)	Benchmark Returns (%)	Composite 3-Yr Annualized Standard Deviation (%)	Benchmark 3-Yr Annualized Standard Deviation (%)	Portfolios in Composite at End of Year	Composite Dispersion (%)	Composite Assets (\$USD Millions)	GIPS Firm Assets (\$USD Millions)
2016	10.5	9.9	12	9.7	10.6	44	0.2	252	30,417
2015	-4.4	-5	1.4	10.1	10.5	53	0.2	331	43,746
2014	11.3	10.7	13.7	8.3	9	72	0.3	446	44,772
2013	29.2	28.5	32.4	8.6	11.9	84	0.3	450	40,739
2012	12.8	12	16	NA	NA	67	0.2	350	26,794
2011	11.6	11	2.1	NA	NA	43	0.2	120	19,962
2010*	6.5	6.5	10.8	NA	NA	8	N/A	22	16,859

*Return is for period October 1, 2010 through December 31, 2010.

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- For the purpose of complying with the GIPS standards, the firm is defined as Brown Advisory Institutional, the Institutional and Balanced Institutional asset management divisions of Brown Advisory. As of July 1, 2016, the firm was redefined to exclude the Brown Advisory Private Client division, due to an evolution of the three distinct business lines..
- The Equity Income Composite includes all discretionary portfolios invested in the equity income strategy. The strategy invests primarily in U.S. equities that exhibit above-average dividend yields, dividend growth and return on equity. The minimum account market value required for composite inclusion is \$1.5 million.
- This composite was created in 2010.
- The benchmark is the S&P 500® Index. The S&P 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy. S&P® and S&P 500® are registered trademarks of Standard & Poor's Financial Services LLC. Index returns assume reinvestment of dividends and do not reflect any fees or expenses. An investor cannot invest directly into an index. Benchmark returns are not covered by the report of the independent verifiers. Standard & Poor's, S&P®, and S&P 500® are registered trademarks of Standard & Poor's Financial Services LLC ("S&P"), a subsidiary of S&P Global Inc.
- The dispersion of annual returns is measured by the equal weighted standard deviation of portfolio returns. The composite dispersion is not applicable (N/A) for periods where there were five or fewer accounts in the composite for the entire period.
- Gross-of-fees performance returns are presented before management fees but after all trading commissions. Net-of-fee performance returns reflect the deduction of actual management fees and all trading commissions. Other expenses can reduce returns to investors. The standard management fee schedule is as follows: 0.80% on the first \$10 million; 0.65% on the next \$15 million; 0.50% on the next \$25 million; and 0.40% on the balance over \$50 million. Further information regarding investment advisory fees is described in Part II A of the firm's form ADV. Actual fees paid by accounts in the composite may differ from the current fee schedule.
- The three-year annualized ex-post standard deviation measures the variability of the composite (using gross returns) and the benchmark for the 36-month period ended on December 31. The three-year annualized standard deviation is not presented as of December 31, 2010, 2011 and 2012 because 36 monthly returns for the composite were not available (N/A).
- Valuations and performance returns are computed and stated in U.S. dollars. All returns reflect the reinvestment of income and other earnings.
- A complete list of composite descriptions, policies for valuing portfolios, calculating performance and preparing compliant presentations is available upon request.
- Past performance does not indicate future results.
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