

# Large-Cap Sustainable Growth

## QUARTERLY STRATEGY UPDATE

Second Quarter 2018

### COMPOSITE PERFORMANCE (%)

	COMPOSITE GROSS OF FEES	COMPOSITE NET OF FEES	RUSSELL 1000® GROWTH INDEX
3 MOS.	5.96	5.83	5.76
YTD	10.84	10.54	7.25
1 YR.	24.54	23.87	22.51
3 YR.	17.15	16.53	14.98
5 YR.	17.79	17.15	16.36
ITD (12/31/2009)	16.96	16.38	15.05

The composite performance shown above reflects the Brown Advisory Large-Cap Sustainable Growth 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

	LARGE-CAP SUSTAINABLE GROWTH REP. ACCT.	RUSSELL 1000® GROWTH INDEX
Wtd. Avg. Market Cap.	\$186.4 B	\$275.6 B
EV/FCF Ratio (FY2 Est.)	24.1x	24.5x
Name Turnover (3 YR Avg.)	22.9%	--

### REP. ACCOUNT TOP 10 PORTFOLIO HOLDINGS

SECURITY	% PORTFOLIO
Microsoft Corp.	5.0
Visa, Inc.	4.7
Alphabet, Inc. (Class A & C)*	4.5
Amazon.com, Inc.	4.5
UnitedHealth Group, Inc.	4.4
American Tower Corp.	4.3
Thermo Fisher Scientific, Inc.	3.8
Intuit, Inc.	3.7
Adobe Systems, Inc.	3.7
Danaher Corp.	3.6
<b>TOTAL</b>	<b>42.2</b>

\*Alphabet Inc. represents a 4.0% holding position in class A and 0.6% in class C shares of the stock.

## Review & Outlook

The strategy outperformed its benchmark, the Russell 1000® Growth Index, during the second quarter. Strong stock-specific performance in health care, industrials and information technology offset declines among our holdings in materials and real estate. In terms of sector allocation, our underweight in consumer discretionary was a drag on performance this quarter, while our underweight in financials was a benefit to our relative return.

As of the date of this writing, U.S. equity markets remain strong despite worrying factors such as the strengthening dollar, commodity price inflation and potential blowback from shifting U.S. trade policy. Our focus, as always, is on companies with strong fundamentals and sustainability strategies that are driving strong financial performance; we are always careful to avoid chasing momentum—especially so in environments such as the current one.

Technology was once again a major positive driver of performance this quarter. **Visa**, **Intuit**, **Salesforce** and **Monolithic Power** all reported results ahead of consensus expectations; these results generated a strong positive lift to our portfolio, given our overall concentrated approach to investing as well as our confidence in each of these companies as long-term holdings. Within health care, **West Pharmaceuticals**, **UnitedHealth** and **Idexx Laboratories** all had strong quarters—each did well for reasons specific to their business models, and additionally they all benefited from strong outlooks within their respective end markets.

While many investors are focused on valuation in the broader market, we are more concerned with whether any one of our companies has peaked in its growth rate—we are generally more cautious when valuations are stretched, but growth is still an essential success factor for our investments. We seek out opportunities where growth is accelerating and where we believe investors will continue to reward companies for excellent execution, even if broader market sentiment wanes a bit. Intuit, for example, is now benefiting from multiyear investments in its One Ecosystem platform, and its leadership in tax and accounting software now gives it an unrivaled value proposition in a growing market of tech-savvy do-it-yourself tax filers. **Danaher's** core business is also accelerating organically; its M&A opportunities and strong product introductions provide additional avenues for it to grow and expand its margins.

Trading activity was somewhat elevated this quarter as we sought to actively manage position size in a somewhat frothy environment. We took advantage of temporary weakness to increase portfolio weights in **Ball**, **Fortive**, **American Tower** and **Marvel Technologies**, among others. To fund these adds, we trimmed several names after strong performance runs, including **Adobe**, **Intuit**, **Amazon** and **Red Hat**.

We also initiated two new positions in **Marriott International** and **Autodesk**. Marriott is the world's largest branded hotel network, a position solidified by its recent acquisition of Starwood Hotels. With consolidation increasing in the hotel market, we believe that share will accrue to the largest chains. The company enjoys structurally high returns on invested capital, given its asset-light franchise model; meanwhile, its franchisees benefit from lower distribution, procurement and marketing costs due to Marriott's global scale. Marriott has long been an industry leader in terms of environmental management, and its track record on that front has increasingly made it a preferred partner for large corporate customers in addition to helping them reduce costs over time.

Autodesk is a provider of computer-aided design (CAD) software, with an entrenched position in the architecture, manufacturing, media and entertainment industries. We believe these end markets have growing needs for engineering software, and customers tend to remain loyal due to embedded education and training programs, the vast number of legacy designs made with the software and the substantial switching costs due to process automation and data formatting. Autodesk's software is often essential in its customers' efforts to address demand for sustainable design.

We remain fully invested and disciplined in our process of finding investment opportunities at the intersection of strong fundamentals, sustainable business advantages and attractive valuation. This philosophy has served us well over the last eight years, and we believe it will continue to do so in the years ahead. [LE](#)

**KARINA FUNK, CFA**  
Portfolio Manager

**DAVID POWELL, CFA**  
Portfolio Manager



## Sector Diversification

- Sector allocation in both absolute and relative terms did not change significantly during the quarter.
- Consistent with prior quarters, the portfolio is overweight industrials and underweight consumer staples, energy and financials. We do not use sector rotation as a driver of return; our sector weightings are primarily determined by where we find opportunities in our bottom-up stock selection process.
- As we have previously noted, many of our industrial and information technology holdings could be categorized within other sectors. Several of our industrial firms primarily serve in the health care sector, while some technology holdings are involved in financial services.

SECTOR	LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT (%)	RUSSELL 1000® GROWTH INDEX (%)	DIFFERENCE (%)	LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT (%)	
	Q2 '18	Q2 '18	Q2 '18	Q1 '18	Q2 '17
Consumer Discretionary	13.42	17.96	-4.54	12.51	8.45
Consumer Staples	2.20	5.72	-3.52	2.93	4.52
Energy	--	1.01	-1.01	--	--
Financials	--	4.44	-4.44	--	--
Health Care	21.31	13.37	7.95	21.32	19.17
Industrials	14.90	11.76	3.14	17.10	19.97
Information Technology	38.49	41.63	-3.14	36.75	37.26
Materials	5.25	1.80	3.45	4.97	6.11
Real Estate	4.44	2.16	2.27	4.43	4.52
Telecommunication Services	--	0.15	-0.15	--	--
Utilities	--	--	--	--	--

## Quarterly Attribution Detail by Sector

- Although we experienced a good deal of dispersion in returns among our technology holdings, the group as a whole performed well.
- Strong quarters for West Pharmaceuticals, UnitedHealth and Idexx Laboratories bolstered our health care results. Other health care holdings, like Danaher, **Thermo Fisher Scientific**, **Mettler-Toledo** and **Edwards**, were all flat to slightly up during the quarter, after major contributions to our returns over the several quarters prior.
- The materials sector was a drag on returns due to weak results from **Ecolab** and Ball Corporation. Ecolab issued an essentially inline earnings report, and while it faces understandable concerns about commodity inflation, we believe it can pass those costs on and expand margins, albeit with a lag. Ball Corporation is challenged by factors outside of the company's control, which we discuss later in this report.
- Within industrials, **Welbilt** delivered a strong quarter, which was partly offset by weak results from **Nordson** due to that company's exposure to the electronics supply chain. **Healthcare Services Group** also suffered from worsening end market conditions; we sold out of this name during the quarter

SECTOR	LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT		RUSSELL 1000® GROWTH INDEX		ATTRIBUTION ANALYSIS		
	AVERAGE WEIGHT (%)	RETURN (%)	AVERAGE WEIGHT (%)	RETURN (%)	ALLOCATION EFFECT (%)	SELECTION AND INTERACTION EFFECT (%)	TOTAL EFFECT (%)
Consumer Discretionary	12.81	10.31	18.80	9.66	-0.22	0.06	-0.16
Consumer Staples	2.55	-0.45	5.96	0.61	0.16	0.02	0.18
Energy	--	--	0.87	9.64	-0.04	--	-0.04
Financials	--	--	3.51	-0.08	0.21	--	0.21
Health Care	21.23	6.40	12.54	5.22	-0.05	0.25	0.20
Industrials	15.59	0.16	12.22	-2.82	-0.29	0.38	0.09
Information Technology	38.26	9.93	39.71	8.61	-0.04	0.46	0.43
Materials	5.45	-2.37	3.27	2.93	-0.04	-0.29	-0.33
Real Estate	4.11	0.29	2.28	5.06	-0.01	-0.20	-0.21
Telecommunication Services	--	--	0.83	3.68	0.02	--	0.02
Utilities	--	--	0.01	1.70	--	--	--
<b>Total</b>	<b>100.00</b>	<b>6.15</b>	<b>100.00</b>	<b>5.76</b>	<b>-0.29</b>	<b>0.68</b>	<b>0.39</b>

Please see disclosure statements at the end of this presentation for additional information and for a complete list of terms and definitions.

## Quarterly Contribution to Return

- Intuit preannounced its third quarter 2018 results, and its results topped already elevated expectations. Revenue growth continues to accelerate across its business and consumer segments. We added to this position earlier this year and recently trimmed after the stock's strong response to these results.
- Amazon is on a strong path. The company announced a 20% price hike for membership in its Amazon Prime program and, given the loyalty of its membership base, this represents a meaningful flow-through to its bottom line. Amazon also made headlines with its acquisition of PillPack, an innovative mail-order pharmacy. The company has been laying the foundation for strong growth and additional opportunities in what are yet nascent businesses, like pharmaceutical supplies and advertising, in addition to the impressive core growth it is generating in e-commerce and Amazon Web Services. We trimmed our position on strength to manage position size.
- UnitedHealth reported solid execution across the board in the first quarter and raised guidance for the rest of its fiscal year. The company's Optum data analytics capabilities provide value-added health care insights, and we believe the fundamentals of its Medicare and Medicaid businesses are poised for a strong year of expanding membership and margins.
- Adobe Systems exceeded expectations once again by delivering strong revenue growth, margin expansion and free cash flow generation. We trimmed our position on this strength to maintain our preferred position size. Adobe remains a core holding in the portfolio.
- Visa delivered a beat to consensus numbers and increased its guidance for the year. We believe the company will benefit from strong secular drivers in the global payments (digital and mobile) markets for years to come. We trimmed our position slightly to make room for new holding Autodesk.
- Red Hat had been among our top performers since the beginning of the year, and we had been trimming it on strength. In its latest earnings release, the company disappointed investors with soft guidance. Currency exchange is one headwind that we see as temporary, and the maturing of its legacy middleware business is still consistent with our growth thesis, which is focused on application development using containers.
- Healthcare Services Group took an unusual receivables write-down during the quarter, reflecting the dire condition of its end market. While the company's services can save customers money regardless of market conditions, the challenged financial conditions of skilled nursing and rehabilitation facilities render Healthcare Services Group's cash flows unreliable at this time. We exited the position and reallocated capital to Autodesk, where we see more upside.
- Ball Corporation has been troubled by overall weakness in the North American beer market, upcoming capacity adds by competitors in Latin America and a trucker's strike in Brazil late in the quarter. The company also announced plans to sell the slowest-growing portion of its portfolio—its steel food and aerosol can assets—to form a joint venture with a global private equity firm that will be called Ball Metalpack. We added to our small position with confidence in the company's capital allocation strategy and the innovations we believe it can deliver.

LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT TOP FIVE CONTRIBUTORS				
TICKER	NAME	AVG. WEIGHT (%)	RETURN (%)	CONTRIBUTION TO RETURN (%)
INTU	Intuit Inc.	3.85	18.13	0.67
AMZN	Amazon.com, Inc.	4.33	17.44	0.66
UNH	UnitedHealth Group Incorporated	4.43	15.05	0.63
ADBE	Adobe Systems Incorporated	4.17	12.83	0.55
V	Visa Inc. Class A	4.86	10.90	0.52
LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT BOTTOM FIVE CONTRIBUTORS				
RHT	Red Hat, Inc.	3.23	-10.13	-0.21
HCSG	Healthcare Services Group, Inc.	0.59	-11.82	-0.21
BLL	Ball Corporation	2.08	-10.23	-0.20
AOS	A. O. Smith Corporation	2.60	-6.71	-0.16
NDSN	Nordson Corporation	2.09	-5.59	-0.12

- **A.O. Smith** reported a solid quarter and raised guidance. However, the stock came under pressure due to concerns about the trade war between the U.S. and China. While 34% of company revenues come from the Chinese market, all of its China sales are sourced and manufactured locally, and thus will not be subject to tariffs between the U.S. and China.
- Nordson reported solid second-quarter results, but guidance was below consensus expectations. We had trimmed our position aggressively earlier in the quarter given the tough comps versus last year due to tailwinds in its sales to mobile device markets that will not repeat. We added back to the position within the quarter after we saw consensus numbers become more reasonable and evidence that the rest of its business is solidly growing by mid-single digits.

## Portfolio Activity

- Autodesk designs and distributes software applications for the architecture, engineering and construction industries. The company is in the midst of a business model transition that we believe will be positive for the stock over the long term. Autodesk is moving away from selling its software via license to selling its software on a subscription basis. It is also emphasizing direct sales versus the channel to increase profitability. From a fundamental perspective, Autodesk has worldwide brand recognition and an industry-leading installed base. The company's business model is strong with high recurring revenue and low capital intensity. As the world's largest design software company, Autodesk's vision is to help people design and create a better world. Its Building Information Modeling (BIM) software helps create sustainable buildings and reduce waste in the construction process.
- Marriott is the world's largest hotel company. In 2016, Marriott acquired Starwood Hotels and Resorts, thereby combining multiple leading hospitality brands and properties. We believe the deal makes Marriott much stronger in its ability to negotiate with the online travel reservation companies. The fundamental underpinnings of Marriott's business model are strong—Marriott is a fee-based company with limited capital intensity and high margins. Marriott's sustainable business advantage is its proven track record of environmental and social performance, which makes it increasingly attractive to business partners. In 2007, Marriott was the first global hotel chain to calculate its carbon footprint, and the company has the largest number of hotels certified and registered as LEED buildings of any hospitality company worldwide.

LARGE-CAP SUSTAINABLE GROWTH REP. ACCOUNT PORTFOLIO ACTIVITY		
ADDITIONS		SECTOR
ADSK	Autodesk, Inc.	Information Technology
MAR	Marriott International, Inc. Class A	Consumer Discretionary
DELETIONS		SECTOR
HCSG	Healthcare Services Group, Inc.	Industrials
SBUX	Starbucks Corporation	Consumer Discretionary

- We sold our position in **Starbucks** and reinvested the proceeds in Marriott, as we believe that Marriott has more growth potential.
- We also eliminated Healthcare Services Group after losing confidence in the conditions of its end market. The proceeds were reinvested in Autodesk.

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# Large-Cap Sustainable Growth 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)
2017	29.1	28.4	30.2	10.6	10.5	32	0.2	762	33,155
2016	6.6	6.0	7.1	11.5	11.2	32	0.1	503	30,417
2015	13.7	13.1	5.7	11.1	10.7	23	0.3	405	43,746
2014	7.1	6.5	13.1	9.9	9.6	25	0.1	303	44,772
2013	34.5	33.7	33.5	12.1	15.5	24	0.2	288	40,739
2012	16.5	15.9	15.3	15.7	15.7	22	0.3	211	26,794
2011	5.4	5.0	2.6	--	--	21	0.3	37	19,962
2010	23.5	23.1	16.7	--	--	18	--	13	16,859

Brown Advisory Institutional claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Brown Advisory Institutional has been independently verified for the periods from January 1, 1993 through December 31, 2017. The Verification reports are available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation. GIPS® is a registered trademark owned by CFA Institute.

- \*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 Large-Cap Sustainable Growth Composite includes all discretionary portfolios invested in the Sustainable Large Cap Strategy. The strategy invests primarily in large market capitalization companies with financially and environmentally sustainable business models. The minimum account market value required for composite inclusion is \$1.5 million. Prior to 2012, the minimum was \$100,000.
- This composite was created in 2010. Prior to 3/31/13, the strategy was named Large-Cap Sustainability. Prior to 12/31/2011 the strategy was named Winslow Green Large Cap. No changes have been made to the strategy since inception.
- The benchmark is the Russell 1000® Growth Index. The Russell 1000® Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000® Index companies with higher price-to-book ratios and higher forecasted growth values. The Russell 1000® Growth Index is constructed to provide a comprehensive and unbiased barometer for the large-cap growth segment. The Index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect growth characteristics. The Russell 1000® Growth index and Russell® are trademarks/service marks of the London Stock Exchange Group companies. An investor cannot invest directly into an index. Benchmark returns are not covered by the report of the independent verifiers.
- 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, and gross of foreign withholding taxes (if applicable). 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 3 year annualized standard deviation is not presented as of December 31, 2010 and December 31, 2011 because 36 month returns for the composite were not available (NA).
- 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 are available upon request.
- Past performance does not indicate future results.
- This piece is provided for informational purposes only and should not be construed as a research report, a recommendation or suggestion to engage in or refrain from a particular course of action or to make or hold a particular investment or pursue a particular investment strategy, including whether or not to buy, sell or hold any of the securities mentioned, including any mutual fund managed by Brown Advisory.

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Composite performance is based on the Brown Advisory Large-Cap Sustainable Growth Composite and was obtained through FactSet®. All information and returns shown are as of 06/30/2018 for each period. Returns greater than one year are annualized. Past performance is not indicative of future results. Representative account characteristics and top 10 holdings were obtained through FactSet. This information is based on a representative Large-Cap Sustainable Growth account and is provided as supplemental information. Account characteristics exclude cash and cash equivalents; top 10 holdings list includes cash and cash equivalents. FactSet® is a registered trademark of FactSet Research Systems, Inc.

References to specific securities are for illustrative purposes only and do not represent all of the securities purchased, sold or recommended for advisory clients. The security returns listed represent the period of when the security was held during the quarter. Top five and bottom five contributors exclude cash and cash equivalents. Sector diversification and sector attribution excludes cash and cash equivalents. Total portfolio return figures provided reflect the sum of the returns of the equity holdings in the representative account portfolio due to price movements and dividend payments or other sources of income, and exclude cash. Performance figures may vary from actual portfolio performance, as calculations are based on end-of-day security prices and do not incorporate the actual cost basis or sale price of individual securities. Sectors are based on the Global Industry Classification Standard (GICS®) classification system. GICS® is a registered trademark of MSCI and Standard & Poor's Financial Services LLC. The individual amounts shown for top ten holdings, sector diversification and quarterly attribution may not sum to the total amount shown due to rounding.

Please see composite disclosure statements above for additional information.

### Terms and Definitions For Representative Account Calculations

All financial statistics and ratios are calculated using information from FactSet as of the report date unless otherwise noted. **Market Capitalization** refers to the aggregate value of a company's publicly traded stock. **Weighted Average Market Cap** refers to the average of each holding's market cap, weighted by its relative position size in the portfolio (in such a weighting scheme, larger positions have a greater influence on the calculation). **Enterprise Value/Free Cash Flow (EV/FCF)** is the enterprise value of a company (defined as market value plus debt minus cash and minority interests) divided by its free cash flow (defined as operating cash flow minus net capital expenditure). EV/FCF calculations presented use FY2 earnings estimates; FY1 estimates refer to the next unreported fiscal year, and FY2 estimates refer to the fiscal year following FY1. **Name Turnover** is the ratio of the lesser of the portfolio's aggregate purchases or sales during a given period, divided by the average value of the portfolio during that period, calculated on a monthly basis. Portfolio turnover is provided for a three-year trailing period. All of the above ratios for a portfolio are expressed as a weighted average of the relevant ratios of each portfolio holding. EXCEPT for P/E ratios, which are expressed as a weighted harmonic average. The **Average Weight** of a position or sector refers to the daily average for the period covered in this report of a stock's value as a percentage of the portfolio. The **Total Return** of an equity security is the sum of the return from price movement and the return due to dividend payments or other sources of income. Standard benchmark-, sector- and portfolio-level returns are the sums of the weights of each security multiplied by its return, summed and calculated daily and summed over the period covered by the report or by an otherwise-noted period. **Allocation Effect** measures the impact of the decision to allocate assets differently than those in the benchmark. **Selection and Interaction Effect** reflects the combination of selection effect and interaction effect. Selection effect measures the effect of choosing securities that may or may not outperform those of the benchmark. Interaction effect measures the effect of allocation and selection decisions (i.e., did we overweight the sectors in which we underperformed). **Total Effect** reflects the combination of Allocation, Selection and Interaction effects. Totals may not equal due to rounding. **Contribution To Return** is calculated by multiplying a security's beginning weight as a percentage of a portfolio by that security's return for the period covered in the report.