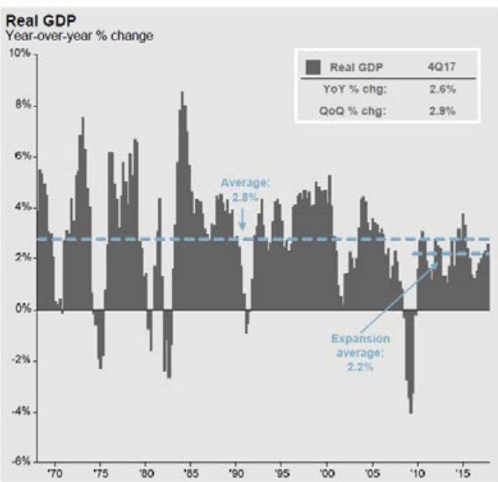
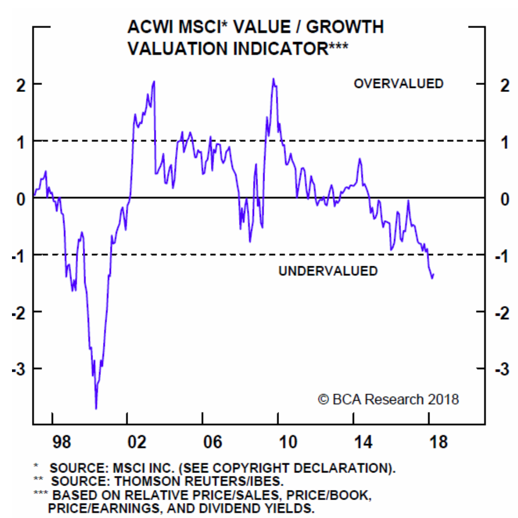
To further our clients' understanding of the investment selections we make for their portfolios, we are introducing a written piece entitled *Portfolio Insights*. To be published in the months between our quarterly *Market Commentary*, this piece is designed to discuss specific constituents of portfolios managed by Heritage Wealth Advisors, their performance and the trends influencing that performance.

In recent years growth stocks have outperformed value stocks to such an extent that the gap between the two has reached extreme levels. While U.S. the economy is enjoying one of its longest expansions on record, the pace of economic growth has been tepid for many years. As the first chart shows, the post-financial crisis expansion average for economic growth has been just 2.2%, below the longer-term average of 2.8%.



As a result, investors have been willing to pay a premium for growth stocks bidding up the price of companies with above-average sales and earnings growth rates—most obviously the FAANG (Facebook, Apple, Amazon, Netflix, Alphabet's Google) stocks--as their performance far outshined most other companies. Value stocks (companies typically with slower growth rates, often economically-sensitive, but also lower valuations) have been left behind as illustrated by the second chart, which depicts the rather large valuation discount that exists today between growth and value, one not seen since the late 1990s just before the bursting of the Technology bubble.



Growth stocks broadly have extended their relative outperformance thus far in 2018. Through the end of April, the Russell 1000 Growth Index was up 2.44% while the Russell 1000 Value Index was down 1.59%.

Value investing targets companies believed to be trading below an estimate of their intrinsic value. An obvious example would be investing in companies that are trading below their stated book value. Another example would be purchasing a stock at an earnings multiple below the estimated earnings growth rate. Value investing may, therefore, be considered a more conservative approach. Moreover, this style of investing inherently requires patience and a long-term view for the market to realize the value that a manager may believe exists in an individual stock. As such, there may periods of underperformance before the potential value is realized. At Heritage, we have a value bias to some of our holdings. In the domestic small cap area for example, we employ Diamond Hill, a value manager.

The Diamond Hill Small Cap fund invests at least 80% of its net assets in U.S. equity securities with small market capitalizations that the fund manager believes are undervalued. Small cap companies are defined as companies with market capitalizations at the time of purchase below $3 billion or in the range of those market capitalizations of companies included in the Russell 2000 Index at the time of purchase. The Russell 2000 Index is a well-established index of small cap stocks that are not included in larger, more well-known indices like the S&P 500.

In the first quarter, the Diamond Hill Small Cap Fund returned -1.0% versus the Russell 2000 Index, which returned -0.1%. Fund performance for a given period can be broken down into different factors, from sector exposure (e.g. energy, industrials, etc.) to selection of specific stocks. When assessing their performance in the first quarter, Diamond Hill noted that both an underweight in healthcare, stock selection in healthcare, and an underweight in technology accounted for the underperformance of the fund. Partially offsetting these detractors was good performance of the technology stocks owned in the fund.

This is to say that relative to the Russell 2000 Index, Diamond Hill had less exposure to healthcare, and the stocks that the manager selected in healthcare lagged the performance of the healthcare sector. Selection of technology stocks helped the fund's performance, but ownership of stocks in technology broadly was less than that of the index.

A manager with a value bias like Diamond Hill will tend to favor certain sectors over others. Favoring stocks with modest valuations can make it challenging to find technology companies, which are often faster growing but trade with lofty valuations, to put in the portfolio. More opportunities may be found in sectors like industrials where, in fact, Diamond Hill has a significant overweighting. The fund is also overweight stocks in the consumer area, both discretionary and staples.

Cash levels in the fund are somewhat high, in the 12%-13% range. It is more typical to see funds with cash levels at 5% or lower. Diamond Hill explains the high cash level due to the current challenge of finding stocks that meet their valuation criteria. Value managers are stingy by nature, and it may not be too surprising that late into an eight-plus year bull market with the stock market near all-time highs that bargains are harder to find.

When compared to the Russell 2000 Value Index--an index that includes companies in the Russell 2000 with value characteristics and therefore a more relevant comparison--, which returned -2.64% in the first quarter, the Diamond Hill Small Cap fund's -1.0% return compares favorably. Last year, the Diamond Hill fund was up 8.25% as compared to an increase of 6.53% for the value index.

Despite the extended period of outperformance for growth stocks, we do not believe that the merits of value investing have diminished and instead feel the pendulum has swung too far in favor of growth stocks. Buying businesses at reasonable prices either directly or through a mutual fund should never go completely out of style.