RIDGEWORTH INSIGHTS: GROWTH EQUITY

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RIDGEWORTH FUNDS

RidgeWorth Large Cap Growth Stock
RidgeWorth Small Cap Growth Stock

EXECUTIVE SUMMARY

- Growth underperformed value as investors grew wary of risk assets.
- The United Kingdom's (UK) vote to exit the European Union (EU) led to a spike in volatility and was particularly challenging for large cap growth stocks.
- Growth-oriented investors must adjust to the lower absolute growth typical of the final stages of an economic cycle.

Growth stocks rose modestly for the second quarter of 2016, underperforming value stocks and the broader equity markets. The Russell 1000 Growth Index returned 0.61%, compared to a 4.58% gain for the Russell 1000 Value Index and a 2.46% return for the S&P 500 Index. Small cap growth stocks fared better than their large cap counterparts, although they underperformed small cap value stocks. The Russell 2000 Growth Index posted a 3.24% return, compared to a gain of 4.31% for the Russell 2000 Value Index.

Two trends dominated the story of the quarter in growth equities: Investors favored small caps over large caps and defensive stocks over risk assets. Investors lost their appetite for risk due to tepid economic growth. A weak report on first quarter U.S. gross domestic product growth stoked fears of a recession—which has never been far from investors' minds throughout the current ongoing economic recovery. For much of the period, the Federal Reserve Board (Fed) seemed likely to raise interest rates, compounding worries about future growth.

A weak jobs report in May stoked investors' fears about the economy. That said, the May jobs report led the Fed to delay its widely anticipated interest rate increase, which helped reassure investors. On balance, however, the markets seemed to interpret the weak job numbers as bad news, as investors flocked toward the perceived safety of U.S. Treasuries and away from risk assets such as growth-oriented stocks.

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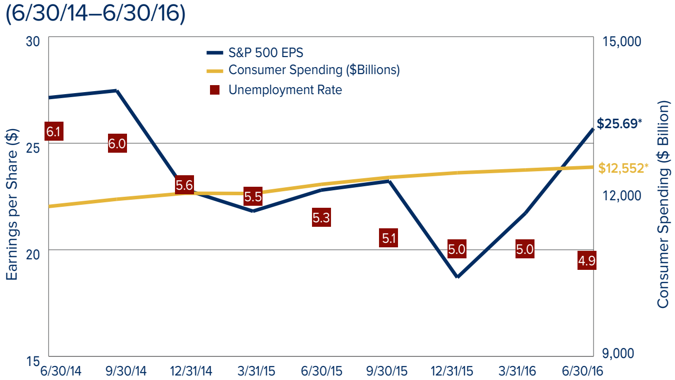
The UK's vote to leave the EU late in the quarter surprised the markets and triggered a large spike in volatility. The outcome of the Brexit vote was challenging for growth stocks, and particularly for large cap growth stocks. The vote created additional uncertainty about the growth prospects of a major economic zone that is already struggling. Europe is a major source of earnings for large U.S. companies, thus larger companies were particularly exposed to the fallout from the referendum.

Some positive economic factors during the quarter helped temper investor pessimism. In particular, crude oil prices rose from an April low of $34 a barrel to top $51 in early June.[1] Rising oil prices helped drive strong gains in the Energy sector. This trend benefited value investors more than it did growth investors; Energy is heavily represented in the Value Index but has little weight in the Growth Index. Consumer spending also rose at the start of the quarter,[2] which helped shore up investor sentiment after weak first quarter spending numbers. Meanwhile, S&P 500 earnings estimates appeared to level out after trending downward for the previous few quarters.[3] Although it is not clear if earnings will rise going forward, the stabilization of earnings may be a positive sign for growth-oriented stocks should the economy remain on track for the rest of the year.

Exhibit 1: EPS, Unemployment Rate and Consumer Spending (6/30/14–6/30/16)



Sources: S&P Dow Jones Indicies, Bureau of Labor Statistics, Bureau of Economic Analysis, U.S. Dept of Commerce; Date pulled: 7/21/16.
*6/30/16 number is estimated

[1] St. Louis Fed. Price based on WTI. (https://fred.stlouisfed.org/graph/?id=DCOILWTICO,)

[2] Bureau of Economic Analysis (http://www.bea.gov/newsreleases/national/pi/pinewsrelease.htm)

[3] S&P 500 Earnings and Estimate Report (July 13, 2016) (https://us.spindices.com/documents/additional-material/sp-500-eps-est.xlsx)

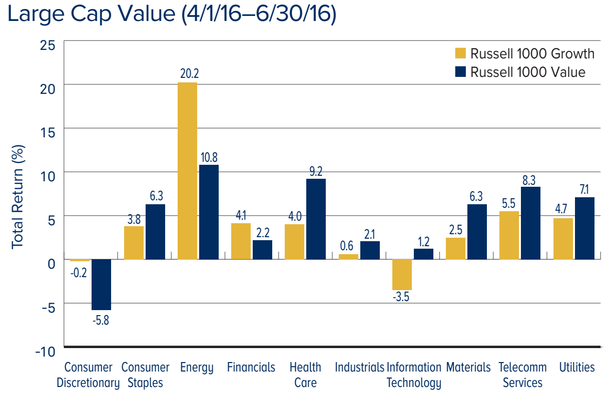
In this environment, defensively oriented sectors such as Utilities, Telecommunication Services and Consumer Staples performed well, while more aggressive sectors such as Information Technology and Consumer Discretionary fared poorly.

GROWTH STRUGGLED AT ALL LEVELS

Within most sectors, growth-oriented stocks underperformed their value-oriented counterparts. Among large cap healthcare stocks, for example, higher-growth biotechnology stocks suffered from the general lack of appetite for risk assets. Investors were wary of the impacts that the politics of price controls might have on the drug industry, and of the continuing fallout from a pricing scandal at a major pharmaceutical company. By comparison, slower-growing healthcare stocks, namely those in the healthcare equipment and supplies industry, performed strongly for the quarter as investors sought out the relative safety of this segment.

Technology stocks offer another such example. The Russell 1000 Value Index's technology stocks posted a small positive return, while the Russell 1000 Growth Index's tech holdings ended the quarter with a 3.5% loss. In this case, much of the underperformance was driven by weakness in the hardware industry—a relatively high-growth segment. Apple, which accounts for a large percentage of the Index's technology weighting, suffered through a weak quarter in which growth showed signs of slowing, leading investors to reevaluate their expectations and causing the share price to fall.

Exhibit 2: Sector Performance – Large Cap Growth vs. Large Cap Value (4/1/16–6/30/16)



Source: FactSet; Date pulled: 7/11/16.

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Companies in the Technology sector's fast-growing communications equipment segment also were hurt by lowered expectations. In one instance, a network and enterprise security company grew in-line with expectations, but investors were disappointed because they had become accustomed to the company consistently exceeding expectations. The company's share price plunged as a result.

The difference between growth and value was less pronounced among small cap stocks. There are many industries in which value investors favor large caps, but growth-oriented investors target small caps. For example, among healthcare services and equipment and supply stocks, large caps tend to appeal to value investors while small caps tend to attract growth investors. Smaller companies in these industries typically target specific niches, where they have greater opportunity to grow without confronting the degree of competition faced by larger companies.

Small cap financial stocks also fared well, despite lower interest rates and the Fed's decision not to raise the federal funds rate. Loan growth among smaller banks remains healthy. Perhaps more important, the rise in oil prices eased fears that smaller, regional banks would suffer steep losses from bad loans to small oil companies. Small bank stocks had suffered steep declines in late 2015 and early 2016 on fears that crashing oil prices would lead to bankruptcies among small oil firms. As the oil prices rebounded, these stocks recovered.

SEEKING OPPORTUNITIES

We continue to see opportunities for growth, despite the challenging environment. Identifying these opportunities requires acknowledging that the economic cycle is entering its later stages and growing more slowly. That change requires a shift in strategy. Going forward, we expect to see more opportunities among companies that offer lower absolute growth but can outperform market expectations.

These opportunities are everywhere, but among larger companies we find them most often in the Healthcare, Consumer Discretionary and Industrial sectors. By comparison, we tend to find these types of stocks less frequently in the Technology and Consumer Staples sectors. Stocks in the latter sectors tend to be more expensive later in the economic cycle, making it harder for us to find opportunities in which a company is likely to exceed expectations. Large cap tech stocks often have a winner bias: when a large company succeeds in winning significant market share, the benefits are priced in quickly, shrinking the likelihood of beating expectations in the future. A slightly different pattern emerges among small cap stocks. It tends to be easier to find opportunities among small companies in the Consumer Discretionary and Technology sectors. The reason, particularly in the Tech sector, relates to the niche-based strategies of many smaller companies. For example, a small tech company can establish itself in a particular area and then work to expand its market share gradually. To succeed, it does not need to become the heavyweight in its niche. It merely needs to keep growing its market share over time—something that is easier for a small company than for a large company over a long, slow-growth period.

MARKET OUTLOOK

Many fixed income investors' interest rate outlook is "lower for longer." The same may be true for equity returns; that is, investors can expect lower-than-normal returns for a relatively long time. There is no sign that stock market returns will pick up appreciably in the near-term, because the market is not cheap and growth is showing signs of slowing. Yet, neither are there signs that markets are in danger of a large downturn. The economic data does not suggest significantly faster growth, nor does it indicate we're on the verge of a recession. Conditions going forward appear to match what we've seen for most of the recovery to date: tepid growth.

However, there is always room for the unexpected. While inflation remains under control and oil prices have risen, those trends could change. Interest rates may rise at the end of the year. Although the Fed has been clear in its intentions to avoid aggressive hikes, global or domestic factors could force the Fed to change its plans once again. Job growth seems to have slowed, but that's to be expected with a low unemployment rate. Changes in any one of these factors may not be enough to push the system one way or another, but surprise changes can cause the markets to react, driving up volatility. Until a few of these factors start changing, and with a clear direction, the status quo may rule the day.

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Russell 1000 Growth Index is an unmanaged index composed of securities in the Russell 1000 Index, with higher than average price-to-book ratios and higher than average forecasted growth values.

Russell 1000 Value Index is composed of the securities in the Russell 1000 Index with a lessthan- average growth orientation. Companies in this index generally have low price-to-book and price-to-earnings ratios, higher dividend yields, and lower forecasted growth values.

Russell 2000 Growth Index is composed of the securities found in the Russell 2000 Index with a greater-than-average growth orientation. Companies in this index tend to exhibit higher price-to-book and price-to-earnings ratios.

Russell 2000 Value Index is an unmanaged index which is composed of the securities in the Russell 2000 Index with a less-than-average growth orientation. Companies in this index generally have low price-to-book and price-to-earnings ratios.

Standard & Poor's 500 (S&P 500) Index is an unmanaged index of 500 selected common large capitalization stocks (most of which are listed on the New York Stock Exchange) that is often used as a measure of the U.S. stock market.

Investors cannot invest directly in an index.

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Gross Domestic Product (GDP) refers to the market value of all final goods and services produced within a country in a given period. GDP per capita is often considered an indicator of a country's standard of living.

Investment Risks:

Equity securities (stocks) may be more volatile and carry more risk than other forms of investments, including investments in high grade fixed income securities. The net asset value per share of a fund will fluctuate as the value of the securities in the portfolio changes. Growth stocks typically are sensitive to market movements because their market prices tend to reflect future expectations. When it appears those expectations will not be met, the prices of growth stocks typically fall. Small capitalization funds typically carry additional risks since smaller companies generally have a higher risk of failure.

The views expressed herein are as of the quarter-end specified. This information is general in nature, provided as general guidance on the subject covered, and is not intended to be authoritative. It is subject to change without notice as market conditions change, and is not intended to predict the performance of any individual security, market sector, or RidgeWorth Fund. All information contained herein is believed to be correct, but accuracy cannot be guaranteed. Investors are advised to consult with their investment professional about their specific financial needs and goals before making any investment decision.

Before investing, investors should carefully read the prospectus or summary prospectus and consider the fund's investment objectives, risks, charges and expenses. Please call 888.784.3863 or visit ridgeworth.com to obtain a prospectus or summary prospectus, which contains this and other information about the funds.

ABOUT RIDGEWORTH INVESTMENTS

RidgeWorth Investments—a global investment management firm headquartered in Atlanta, Georgia, with approximately $37.0 billion in assets under management as of June 30, 2016—offers investors access to a select group of boutique investment managers and subadvisers. RidgeWorth wholly owns three boutiques: Ceredex Value Advisors LLC, Seix Investment Advisors LLC and Silvant Capital Management LLC, and holds a minority ownership in Zevenbergen Capital Investments LLC. WCM Investment Management and Capital Innovations, LLC serve as subadvisers to the RidgeWorth Funds. Through these six investment managers, RidgeWorth offers a wide variety of fixed income and equity disciplines, providing investment management services to a growing client base that includes institutional, individual and high net worth investors.

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ABOUT SILVANT CAPITAL MANAGEMENT LLC

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