Upgraded to Gold.
By Thomas Lancereau 5/29/2019

A long-tenured manager, sensible and proven process, and reasonable fees make JPMorgan Equity Income one of the best of its kind, supporting an upgrade of its Morningstar Analyst Rating to Gold from Silver.

Manager Clare Hart focuses on companies with attractive dividend yields (at least 2% at purchase), but she places equal attention to low payout ratios as she thinks companies paying out too much income might lack cash for future growth. As such, she sticks to high-quality companies, which she defines as those with durable franchises, a consistent earnings stream to support the payout, high returns on invested capital, conservative financials, and strong management.

As a result, this strategy’s income might not consistently rank in the top quartile of the large-value Morningstar Category. It has actually ranked in the second quartile since 2015. However, what the strategy gives up in yield, it has gained in total return. Since Hart took over in August 2004 through April 2019, the strategy’s Institutional share class has beaten its Russell 1000 Value Index benchmark and typical category peer by 130 and 230 annualized basis points, respectively.

The strategy also has Below Average Morningstar Risk scores, and it has outperformed the index and its peers on a risk-adjusted basis, too. Hart doesn’t prioritize risk control per se and attributes lower volatility to a high-quality portfolio. The portfolio therefore tends to exhibit higher valuation metrics than peers and the benchmark, but it has stronger cash flow growth and a higher net margin and return on equity. Further evidence of Hart’s focus on quality is given by the proportion of stocks with wide Morningstar Economic Moat Ratings, which stand at 52.8% of assets versus 35.6% in the index. She pays attention to price risk and started to trim exposure to some financial services and technology stocks in May 2018 on valuation grounds. These moves and the portfolio’s resiliency paid off in 2018, when the strategy lost 4.5% and outperformed 88% of its peers. Moreover, fees are reasonable, which gives the strategy an edge for the long term.

Process Pillar: Positive
This proven, quality-oriented approach to equity income investing earns a Positive Process rating. Manager Clare Hart has successfully executed it for 15 years, with a consistent and distinctive focus on high-quality companies that are able to sustain a stable dividend and are trading at reasonable valuations.

Hart focuses on companies with attractive dividend yields (at least 2% at purchase), but she places equal attention to low payout ratios as companies paying out too much income might offer great dividend yields today but lack cash for future growth. As such, she sticks to high-quality companies, which she defines as those with durable franchises, consistent patterns of earnings (so that a company can support its payout even in difficult markets), high return on invested capital, conservative financials, and strong management.

Valuation is critical to buy and sell decisions; Hart considers a variety of metrics such as free cash flow yields and P/E, depending on a particular stock.

The fund is benchmarked against the Russell 1000 Value Index, but sectors can range within 10 percentage points of the benchmark weightings, and individual position size is not constrained by benchmark weightings. The portfolio is diversified across around 80-110 holdings, primarily large caps. Hart’s investment style is patient, resulting in low portfolio turnover and transaction costs.

In keeping with the approach that seeks to secure the dividend rather than maximize it, the fund’s dividend yield of 2.8% was just in line with the index and even lower than its typical rival (2.9%) as of March 2019. While the portfolio overall had higher valuations than its benchmark, it also had stronger cash flow growth and a higher net mar-

Morningstar’s Take
Morningstar Analyst Rating  Gold

Morningstar Pillars
Process Positive
Performance Positive
People Positive
Parent Positive
Price Positive

Morningstar Analyst Rating
Morningstar evaluates mutual funds based on five key pillars, which its analysts believe lead to funds that are more likely to outperform over the long term on a risk-adjusted basis.

 Analyst Rating Spectrum

Fund Performance
Total Return % +/- Category
YTD 10.30  0.83
2018 -4.46  4.07
2017 17.55  1.60
2016 14.84  0.03
2015 -2.31  1.73

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Analysis

Clare Hart’s focus on quality is further evident by the proportion of holdings with wide moats, which, at 52.8% of assets, stands higher than the benchmark’s 35.6%.

That preference for higher-quality companies is visible across long-term top holdings such as Merck MRK in healthcare, Microsoft MSFT in technology, and BlackRock BLK among financials. Financials remains the biggest sector preference at 25% of assets, above the category average and the index. However, Hart trimmed some financial services stocks on valuation in mid-2018, dropping the stake from 30% of assets in early 2018. She also took profits on some technology names, including Apple AAPL, to start new positions in Dover DOV and Parker Hannifin PH in industrials. While consumer staples, utilities, and REITs are common picks for strategies with an income emphasis, they have all remained underweight for some time here relative to the index because of heightened valuations.

**Performance Pillar:** Positive

The strategy’s excellent risk/reward profile over time testifies to the consistent execution of its distinctive process by Clare Hart and earns it a Positive Performance rating. Since Hart came on in August 2004 through April 30, 2019, the Institutional share class has returned an annualized 9.4% versus 8.1% for the Russell 1000 Value Index and 7.1% for the large-value category average.

Over time, the strategy’s income has generally stayed above peers but it has rarely ranked in the top decile. This is largely the result of Hart’s investment style as she seeks a sustainable income stream from healthy companies rather than maximizing yield and compromising on quality. That is evidenced by the fund’s Below Average Morningstar Risk rating, indicating it has had less downside volatility than peers. In 2011 and 2018 for instance, performance ranked in the category’s top quintile.

Hart aims to capture much of the market’s upside while limiting drawdowns. During her tenure, the fund has an upside-capture ratio relative to its benchmark of 90% and a downside-capture ratio of 77%. The Sharpe ratio under Hart’s tenure is 0.69 versus 0.47 for the category average and 0.52 for the benchmark. Those strong results have primarily come from stock selection across a variety of sectors; successful picks in 2018 included CME Group CME in financial services and Microsoft MSFT in technology.

**People Pillar:** Positive

The manager’s long tenure and strong supporting resources earn the strategy a Positive People rating.

Clare Hart has run this strategy since August 2004, having joined JPMorgan in 1999. Two long-tenured analysts are dedicated specifically to Hart’s strategies: Andrew Brandon has 19 years of experience at JPMorgan, and Shilpee Raina has been at the firm for 14 years. In February 2019, Brandon was named a co-manager on Silver-rated JPMorgan Growth and Income VGRIX alongside Hart. That portfolio has significant overlap with this one but includes lower-quality names with improving fundamentals that don’t make the cut into JPMorgan Equity Income.

Hart and her analysts belong to the Value team headed by Larry Playford, as does veteran value manager Jonathan Simon. He is a listed co-manager here though he does not have direct day-to-day responsibility for the strategy. Nevertheless, he has more than $1 million invested here. Simon is the longtime lead manager of JPMorgan Mid Cap Value JAMCX and JPMorgan Value Advantage JVAAX, both Morningstar Medalists. Hart has more than $1 million invested in both JPMorgan Equity Income and JPMorgan Growth and Income alongside shareholders.

She also draws from the research of 25 career analysts in JPMorgan’s core equity team; they average about 10 years at the firm.

**Parent Pillar:** Positive

J.P. Morgan Asset Management boasts long-tenured and strongly aligned portfolio managers who are supported by deep analytical resources. Competitive fees across the board also contribute to the firm’s Positive Parent rating.

The firm’s diverse lineup features many Morningstar Medalists across asset classes and regions. In February 2018, its U.S.-domiciled SmartRetirement target-date series was upgraded to a Morningstar Analyst Rating of Gold, befitting strong underlying resources and processes on both equity and fixed income. On U.S. equities, for instance, experienced managers draw on a core team of more than 20 career analysts, while on their core fixed-income mandates, long-tenured managers are supported by more than 25 credit and securitized analysts based across Columbus, London, and New York. Managers’ compensation factors in 10-year performance where applicable, which exceeds industry standards. Retention rates and managers’ co-investments alongside fund shareholders are above average, and succession planning is generally well handled.

Fees are regularly reviewed downward; funds tend to be cheaper relative to peers in the U.S. than abroad. The firm has refrained from trendy offerings and expanded its passive business recently. It has continued to rationalize its broad lineup otherwise, leading to some mergers and liquidations in Europe in particular.

**Price Pillar:** Positive

The fund’s asset-weighted fees rank in the second cheapest quintile, supporting a Positive Price rating. However, the Select shares, the biggest share class, accounting for around 35% of assets, charge 0.75%, which is only average relative to other large-cap institutional shares. The R6 shares are the second biggest, at around 29% of assets. Their expense ratio of 0.5% is cheaper than 70% of similarly distributed retirement shares.

The next two biggest share classes, A and C, are also competitively priced, with expenses respectively falling into the second and top quintile of their relevant distribution groups. The remainder of the fund’s share classes have below-average expenses, too.
MORNINGSTAR RANKINGS AS OF 3/31/19


MORNINGSTAR RATING AS OF 4/30/19

JPMorgan Equity Income Fund, Morningstar overall rating 5 stars, Class I; Large Value Category; 1114 funds. Three-year rating 4 stars; 1114 funds. Five-year rating 5 stars; 958 funds. Ten-year rating 5 stars; 699 funds. Ratings reflect risk-adjusted performance. Overall Morningstar Rating™ for a fund is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics.

The Morningstar Rating™ for funds, or “star rating,” is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds and separate accounts) with at least a three-year history. Exchanged-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product’s monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five- and 10-year (if applicable) Morningstar Rating metrics. The weights are: 100% three-year rating for 36-59 months of total returns, 60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. Rankings do not take sales loads into account.

ANNUAL OPERATING EXPENSES (%)

<table>
<thead>
<tr>
<th>Gross expenses</th>
<th>Net expenses</th>
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</thead>
<tbody>
<tr>
<td>0.75</td>
<td>0.75</td>
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The Fund’s adviser and/or its affiliates have contractually agreed to waive fees and/or reimburse expenses to the extent Total Annual Fund Operating Expenses (excluding acquired fund fees and expenses, dividend and interest expenses related to short sales, interest, taxes, expenses related to litigation and potential litigation and extraordinary expenses) exceed 0.79% of the average daily net assets. The Fund may invest in one or more money market funds advised by the adviser or its affiliates (affiliated money market funds). The Fund’s adviser has contractually agreed to waive fees and/or reimburse expenses in an amount sufficient to offset the fees and expenses of the affiliated money market funds incurred by the Fund because of the Fund’s investment in such money market funds. This waiver is in effect through 10/31/2019, at which time the adviser and/or its affiliates will determine whether to renew or revise it. The difference between net and gross fees includes all applicable fee waivers and expense reimbursements.

PERFORMANCE

<table>
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<th>(%) as of 3/31/19</th>
<th>1 year</th>
<th>3 years</th>
<th>5 years</th>
<th>10 years</th>
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<tbody>
<tr>
<td>I Shares at NAV</td>
<td>8.24</td>
<td>11.77</td>
<td>9.16</td>
<td>15.14</td>
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<tr>
<td>Russell 1000 Value Index</td>
<td>5.67</td>
<td>10.45</td>
<td>7.72</td>
<td>14.52</td>
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<tr>
<td>Lipper Equity Income Funds Index</td>
<td>6.94</td>
<td>10.60</td>
<td>7.85</td>
<td>13.69</td>
</tr>
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</table>

Lipper Index since inception returns are as of month-end. The performance quoted is past performance and is not a guarantee of future results. Mutual funds have fees that reduce their performance: indexes do not. You cannot invest directly in an index.

Performance quoted is past performance and is no guarantee of future results. Investment returns and principal value will fluctuate, so shares, when sold, may be worth more or less than original cost. Current performance may be higher or lower than returns shown. Call 1-800-480-4111 for most recent month-end performance.

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Must be preceded or accompanied by a prospectus.

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TARGET DATE FUNDS:
The JPMorgan Smart Retirement Funds are target date funds with the target date being the approximate date when investors plan to start withdrawing their money. Generally, the asset allocation of each Fund will change on an annual basis with the asset allocation becoming more conservative as the Fund nears the target retirement date. The principal value of the Fund(s) is not guaranteed at any time, including at the target date. This investment is not a complete retirement program and may not provide sufficient retirement income. There may be additional fees or expenses associated with investing in a Fund of Funds strategy. Asset allocation does not guarantee investment returns and does not eliminate the risk of loss.

RISK SUMMARY: The following risks could cause the fund to lose money or perform more poorly than other investments. For more complete risk information, see the prospectus.

Equity Income Fund: The prices of equity securities are sensitive to a wide range of factors, from economic to company-specific news, and can fluctuate rapidly and unpredictably, causing an investment to decrease in value. There is no guarantee that companies will declare, continue to pay or increase dividends.

Growth and Income Fund: The prices of equity securities are sensitive to a wide range of factors, from economic to company-specific news, and can fluctuate rapidly and unpredictably, causing an investment to decrease in value.

Mid Cap Value Fund: Mid-cap funds typically carry more risk than funds investing in well-established "blue-chip" companies and have historically experienced a greater degree of volatility than the average stock.

Value Advantage Fund: The prices of equity securities are sensitive to a wide range of factors, from economic to company-specific news, and can fluctuate rapidly and unpredictably, causing an investment to decrease in value.

INDEXES: The Russell 1000 Value Index is an unmanaged index measuring the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values. The performance of the Lipper Equity Income Funds Index includes expenses associated with a mutual fund, such as investment management fees. These expenses are not identical to the expenses charged by the Fund. Total return figures (for the fund and any index quoted) assume payment of fees and reinvestment of dividends (after the highest applicable foreign withholding tax) and distributions. Without fee waivers, fund returns would have been lower. Due to rounding, some values may not total 100%.

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There can be no assurance that the professionals currently employed by J.P. Morgan Asset Management will continue to be employed by J.P. Morgan Asset Management or that the past performance or success of any such professional serves as an indicator of such professional’s future performance or success.

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MORNINGSTAR DISCLOSURE:
The Morningstar Analyst Rating is not a credit or risk rating. It is a subjective evaluation performed by the manager research analysts of Morningstar. Morningstar evaluates funds based on five key pillars, which are process, performance, people, parent, and price. Analysts use this five pillar evaluation to determine how they believe funds are likely to perform over the long term on a risk-adjusted basis. They consider quantitative and qualitative factors in their research, and the weighting of each pillar may vary. The Analyst Rating scale is Gold, Silver, Bronze, Neutral, Negative. A Morningstar Analyst Rating of Gold, Silver, or Bronze reflect an Analyst’s conviction in a fund’s prospects for outperformance. Analyst Ratings are continuously monitored and reevaluated at least every 14 months.

For more detailed information about Morningstar’s Analyst Rating, including its methodology, please go to http://corporate1.morningstar.com/AnalystRating/

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