Cooke & Bieler

Q2 2022

Concentrated Value Equity

Overview

The investing environment went from challenging to nearly universally negative during the second quarter as markets struggled to digest rising interest rates, unexpectedly high levels of inflation, and signs of economic deterioration. This troublesome combination caused sentiment to turn overwhelmingly negative as it resurrected unhappy memories of the stubborn stagflation that hampered stocks much of the 1970s. Indeed, the -20% return posted by the S&P 500® Index for the first half of 2022 was its worst since 1962. The damage would have been worse were it not for a late quarter rally spurred by views that the Federal Reserve might turn less hawkish in the face of continuing economic weakness.

The breadth of the decline was all-encompassing, with all major benchmarks showing double digit declines and every sector across those benchmarks down as well. As in the first quarter, rising interest rates continued to negatively impact Growth indices most and market turbulence continued to affect smaller capitalization stocks the most. Among sectors, Consumer Staples, Utilities, and Energy held up relatively well across the market cap spectrum, while Information Technology and Consumer Discretionary stocks tended to lag.

Portfolio Performance & Developments

Cooke & Bieler's Concentrated Value Strategy provided some downside protection during the difficult market environment of the second quarter, returning -11.81% gross of fees (-12.02% net of fees) against a -12.41% return for the Russell 3000® Value Index. This outperformance was driven by stock selection effect, while sector allocation effect detracted from results. Consistent with first quarter trends, selection in Financials led the way, with insurance companies such as Progressive and Arch Capital continuing to provide the greatest benefit. Information Technology holdings also proved resilient, with Arrow Electronics and TE Connectivity performing particularly well on a relative basis. The portfolio's Health Care holdings – in particular Medtronic – were the largest negative offset. Selection results in Consumer Discretionary and Industrials were also negative.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Philip Morris	1.4	9.0	33
Progressive	5.2	2.1	12
Johnson & Johnson	5.4	0.8	-4
ESAB	1.6	-2.4	-6
Becton Dickinson	4.0	-3.8	-16

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Brookfield Asset Mgmt.	7.8	-21.2	-170
State Street	5.7	-28.6	-149
Gildan Activewear	5.2	-22.8	-124
AerCap	5.5	-18.6	-110
Medtronic	4.5	-18.5	-80

Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Concentrated Value institutional portfolio's gross of fees return relative to the Russell 3000® Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's Concentrated Value clients. To obtain the calculation's methodology and a list showing every holding's contribution to the overall account's performance during the quarter, contact your client service representative or email your request to contact@cooke-bieler.com.

Largest Contributors

Philip Morris (PM), a leading global tobacco products manufacturer, was the largest contributor. The company's combustible products exhibited strong pricing power and stable volume trends while its reduced risk product portfolio continued to grow at an accelerated pace, both organically and through the pending acquisition of Swedish Match.

Progressive (PGR), a leading personal auto insurer in North America, was the second-largest contributor. PGR demonstrated strong pricing power, offsetting cost increases.

Johnson & Johnson (JNJ), a leading manufacturer of pharmaceuticals, medical devices, and consumer products, was the third-largest contributor. JNJ's defensive characteristics, including its diverse business model, strong balance sheet, and durable cash flow generation, provided support during the worst of the market's second quarter decline.

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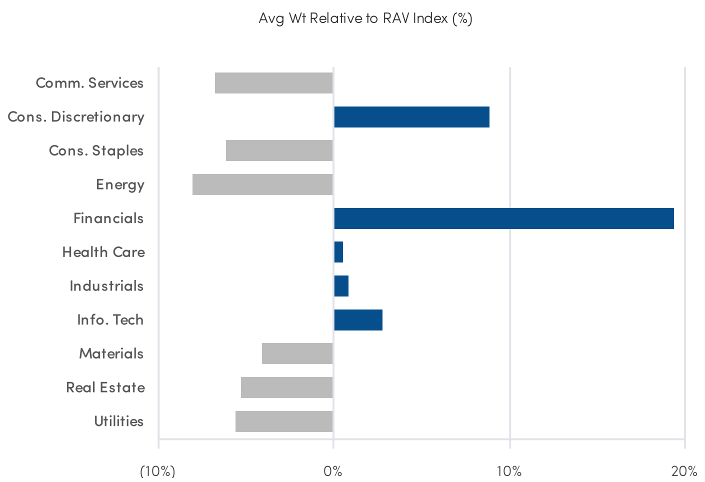
Largest Detractors

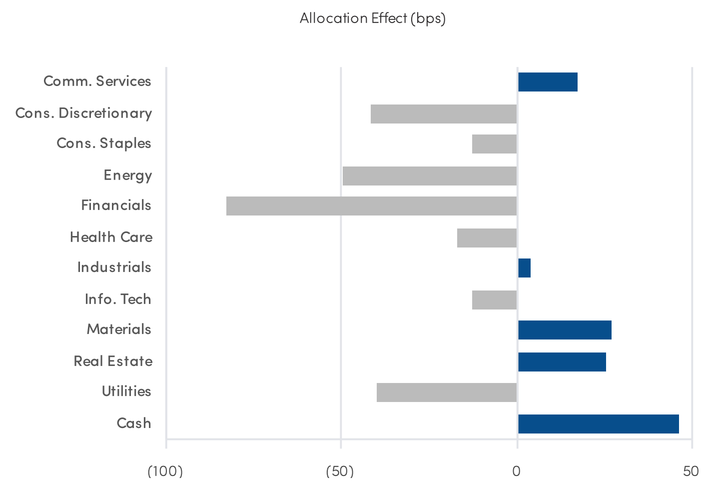
Brookfield Asset Management (BAM), a global investor, operator, and manager of real assets, was the largest detractor. Investor sentiment on the stock waned due to macro concerns of higher interest rates and inflation. BAM is well positioned to benefit from rising inflation while interest rate risk should prove manageable given the company's long-term fixed rate debt. Additionally, the announced spinoff of its asset management business should reduce complexity and better highlight the valuation discrepancies between BAM and its peers.

State Street (STT), a leading custodian and recordkeeper for financial assets, was the second-largest detractor. STT suffered from investor concerns that rising bond yields would have negative implications for its regulatory capital.

Gildan Activewear (GIL), the largest basic apparel manufacturer, was the third-largest detractor. GIL has lagged the overall market as Consumer Discretionary stocks in general have fallen out of favor. However, we believe that investors are failing to sufficiently appreciate the company's improved earnings potential.

Sector Positioning





Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Concentrated Value institutional portfolio's gross of fees sector return relative to the Russell 3000® Value Index. Please see additional performance disclosures at the end of this document.

Sector allocation effect was broadly negative for the second quarter. The portfolio's overweight to Financials and Consumer Discretionary, two of the worst performing sectors within the Index, posed large relative headwinds. Underweight positions in Energy and Utilities – among the benchmark's most defensive sectors during the challenging quarter – also hampered relative results. Conversely, the strategy's underweight positions in Materials, Real Estate, and Communication Services were additive to the portfolio.

Initiations

ESAB (ESAB) is a leading global provider of welding equipment and consumables. The company was spun off from long-time portfolio holding Colfax during the quarter.

Hanesbrands (HBI) is a basic apparel company that sells underwear, intimates, socks, and activewear. The company uses a combination of innovation and brand building to command premium pricing for its products. HBI has a low-cost diversified manufacturing complex which is 90% owned by the company. Management has several options for increasing shareholder value, including organic growth, margin enhancement, and use of cash flow to repurchase shares or pay down debt. We believe HBI's current valuation too aggressively discounts the potential for a slowdown in its fast-growing Champion brand as well as the threat of private label competition.

Stanley Black & Decker (SWK) is an industrial and household tools manufacturer with strong brands and technologies. We believe they should have a significant opportunity to expand distribution in their lawn products segment through their acquisition of MTD Products.

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Eliminations

Becton Dickinson (BDX), **Enovis (ENOV)**, and **Philip Morris (PM)** were eliminated to make room for better opportunities.

Notable Stock Updates

Enovis (ENOV) is the successor entity to long-time portfolio holding Colfax following the spin-off of their welding business. ENOV is a medical technology business selling orthopedic reconstruction, prevention, and rehabilitation products.

Outlook

The end of the second quarter leaves investors worse off and facing the same set of uncertainties that bedeviled them in April. Widespread supply chain disruptions persist, the war in Ukraine seems no closer to resolution, and inflation remains stubbornly high, forcing the Federal Reserve to raise interest rates even as the economy slows. The odds of recession are rising – though the timing and severity remain unclear – and investors' minds are naturally drawn to speculation about when the tide of events will turn. Never long-term oriented or fundamentally focused by nature, most market participants are prone to guessing at geopolitical and economic developments.

We think these inclinations are mistaken. We agree that the Fed's window to engineer a soft landing is shrinking. With the economy already slowing, further monetary tightening risks tipping us into a recession. But with inflation still at multi-decade highs, easing policy too soon risks further embedding inflation and increasing the costs of later action. The Fed's success depends on a myriad of factors mostly out of its control, making their task extremely difficult and investor efforts to predict the outcome futile.

We think it is better to adopt Warren Buffett's mantra of buying good businesses when they go on sale. The trick of course is to distinguish good businesses with low share prices from those that have merely been kept aloft by investor optimism or those that face serious existential threats. This differentiation is the focus of our research: finding businesses that can prosper far into the future regardless of the short-term path of the economy. Recently, this research has led us to find value in Information Technology and Consumer Discretionary companies – businesses left behind as investors worry about rising rates or slowing demand, but which remain poised to earn solid returns over a full cycle. Regardless of the industry or sector, these businesses share strong competitive advantages, conservative capital structures, and talented management teams that we believe can generate attractive returns over the long run. And while their fundamental prospects are largely unchanged, they are all substantially – often 30% or more – cheaper than they were at the beginning of the year. While short-term bumps are inevitable and the market's bottom will only be clear in retrospect, we believe our long-term approach, supported by the conviction that comes from detailed independent research, will add value through this cycle.

Sources: APX, Bloomberg, CNBC, The Economist, FactSet, The New York Times, The Wall Street Journal

Additional Cooke & Bieler Concentrated Value Performance Disclosures