Cooke & Bieler

Q4 2022

Concentrated Value Equity

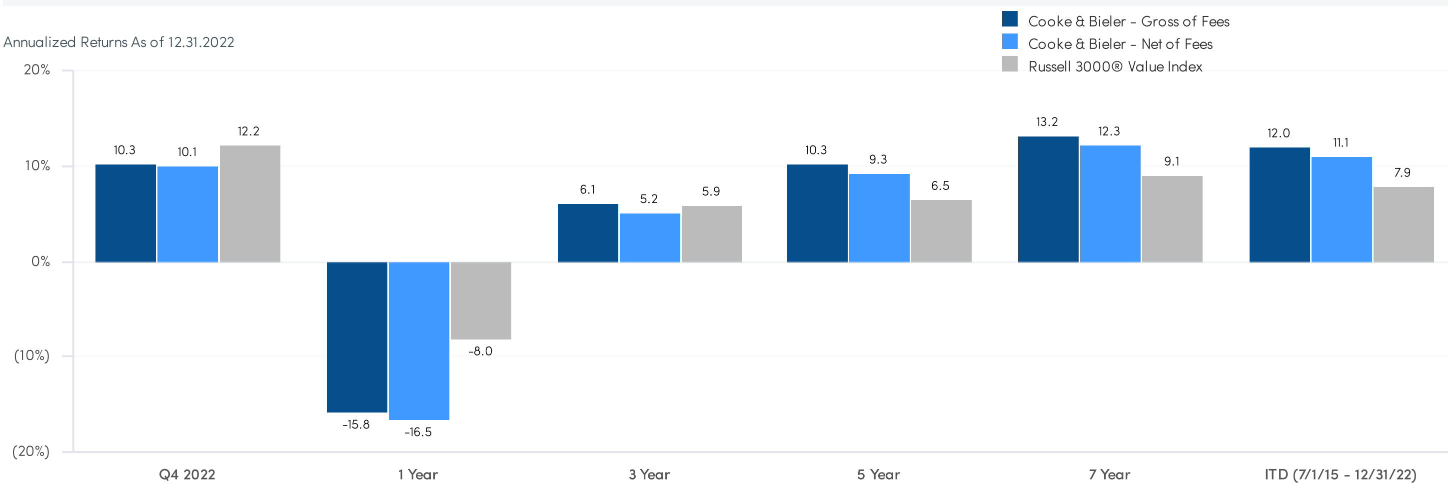
Overview

Stocks recovered strongly in the fourth quarter, but the rally was not strong enough for major indices to avoid their worst calendar year returns since 2008. Improved sentiment was driven by the slower pace of Fed tightening and signs inflation pressures had peaked, with markets also skirting any significant macroeconomic shocks. Oil prices and long-term interest rates ended the quarter broadly flat and the main geopolitical development – China's decision to relax its Covid Zero policy – bodes well for global growth. Domestically, both employment data and consumer spending appeared healthy despite the sharp tightening of monetary conditions since the start of the year, bolstering hopes for a soft landing. Against that backdrop, Energy continued its reign as the best performing sector, while value outperformed growth across the capitalization spectrum for the quarter and the year. Conversely, the most speculative areas of the market, including unprofitable technology companies, cryptocurrency related businesses, and small biotech, posted weak and at times catastrophic returns.

Portfolio Performance & Developments

Cooke & Bieler's Concentrated Value Strategy generated strong absolute Q4 results, though relative performance still lagged for the quarter and full year. During the quarter, the strategy posted a 10.31% return gross of fees (10.10% net of fees) versus a 12.18% return for the Russell 3000® Value Index. This underperformance was due entirely to negative stock selection effect, somewhat offset by positive sector allocation effect. The portfolio's Health Care stocks significantly underperformed the benchmark's sector constituents. Additionally, Consumer Discretionary holdings continued to struggle as investors weighed potential recession scenarios. Conversely, Industrials and Financials holdings contributed most during the quarter.

Concentrated Value Equity Composite Performance



Source: Factset and Russell®

Past performance is not indicative of future results. All investing involves risk, including loss of principal.

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Contributors & Detractors

Largest Contributors

AerCap (AER), the largest independent aircraft lessor, was the largest contributor. AER continued to benefit from the recovery in air travel. In addition, its acquisition of GE's aircraft leasing business has proved accretive to the company's cash flows.

Arch Capital (ACGL), a Bermuda-based specialty property & casualty and mortgage insurer, was the second-largest contributor. ACGL continued to achieve strong operating results, growing its insurance premiums into a hard market environment and compounding book value significantly versus the prior year. Expectations that property catastrophe reinsurance conditions would harden significantly in 2023 also helped the stock's performance. Additionally, investor sentiment on ACGL strengthened due to the stock's inclusion in the S&P 500®.

State Street (STT), a leading custodian and recordkeeper for financial assets, was the third-largest contributor. In addition to showing improved profitability during the quarter, STT demonstrated disciplined use of cash flow as it continued to reduce its share base. Investors also reacted positively to the cancelation of its acquisition of Brown Brothers Harriman's Investor Services business.

Largest Detractors

Syneos Health (SYNH), a leading provider of outsourced pharmaceutical clinical trial and commercialization services, was the largest detractor. The stock's valuation contracted sharply in response to very disappointing new business awards during the quarter and management's cautious outlook for improvement.

Brookfield Corporation (BN), a global investor, operator, and manager of real assets, was the second-largest detractor. Investor sentiment waned in the quarter due to concerns of higher interest rates and liquidity concerns spurred by a competitor's difficulties with a retail-oriented, non-traded REIT product. In addition, the spin-off of 25% of their asset management business added near-term complexity. We continue to believe BN is well positioned, with good fundamental growth opportunities in both its core business and in its 75% stake in the capital-light asset management business.

Brookfield Asset Management (BAM), an asset light manager of alternative assets, was the third-largest detractor. The stock was spun out of its parent company, Brookfield Corporation, late in the quarter during a strong up market.

Sector Positioning

Sector allocation effect was positive for the quarter. The strategy's underweight to Communication Services, the benchmark's worst performing sector, was the largest performance tailwind. An overweight to Industrials and underweight to Real Estate also added to results. Conversely, the portfolio's underweight to Energy, once again the benchmark's best performing sector, continued to weigh on performance and was the largest detractor for the quarter and the year. An underweight Materials position also hindered results.

Initiations & Eliminations

Initiations

Baxter International (BAX) develops, manufactures, and markets a diverse portfolio of lifesaving medical products, including intravenous (IV) solutions and medicines, IV pumps and sets, and peritoneal dialysis solutions and equipment. We believe revenue and margin pressures stemming from the pandemic and input cost inflation should subside as the operating environment normalizes, clearing a path to sustained above average earnings growth.

Eliminations

Brookfield Asset Management (BAM) was spun out of Brookfield Corporation during the quarter and subsequently eliminated, with the proceeds reinvested back into Brookfield Corporation.

Syneos Health (SYNH) was eliminated to make room for better opportunities.

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Notable Stock Updates

Long-term holding **Brookfield Asset Management (BAM)** renamed itself **Brookfield Corporation (BN)** and spun off 25% of its asset management business as a new entity named **Brookfield Asset Management (BAM)**.

Outlook

With an ostensibly better line of sight on the end of the Fed's tightening cycle, investors seemed to focus more on longer-term fundamentals as the year drew to a close. The related underperformance within more speculative areas of the market and greater strength among enterprises with proven business models might presage a more favorable environment for Cooke & Bieler's style of investing. Similarly, it seems many investors who were concerned about a recession are now anticipating a soft landing – a shift in sentiment that benefited many of the portfolio's more cyclical holdings. That said, prevailing macroeconomic forces are likely to keep inflation higher and financial conditions tighter in 2023 and 2024 than they were in the middle part of the last decade, in which case the investing environment will remain challenging, particularly for highly valued stocks. However, we believe the portfolio should be positioned well for either a soft or hard landing due to the strong profitability and healthy balance sheets of our holdings. In addition, many of the more economically sensitive holdings had discounted a long and severe recession going into the fourth quarter. Many of the portfolio's holdings remain egregiously undervalued despite solid long term fundamentals, giving us reason to be optimistic about the portfolio's future prospects.

Sources: Bloomberg, CNBC, CNN, FactSet, NBC, Reuters, U.S. Department of the Treasury

Past performance is not indicative of future results. All investing involves risk, including loss of principal. The material presented represents the manager's assessment of the Concentrated Value institutional portfolio and market environment at a specific point in time and should not be relied upon by the reader as research or investment advice regarding any particular security or sector. The above commentary and portfolio attribution are based on a representative Concentrated Value institutional portfolio for the quarter ending 12/31/22. Certain client portfolios may or may not hold the securities identified above due to the respective account's guidelines, restrictions, required cash flows, or other relevant considerations. The performance attribution is an analysis of the portfolio's 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.

Additional Cooke & Bieler Concentrated Value Performance Disclosures