Large Cap Value Equity

Q1 2022

Overview

Stocks turned in their worst performance since the onset of the pandemic two years ago as investors processed a seeming tsunami of bad news and pushed all major indices into negative territory. The Russian invasion of Ukraine signaled not just the largest European war in 75 years, but perhaps the most aggressive sanctions regime in history. The combination touched off a price surge in oil and other commodities, further fueling inflationary trends that were already running at 40-year highs and sending 10-year treasury yields to their highest level in two years. Recent history would suggest the Federal Reserve would react to these shocks by communicating their ability and willingness to ease monetary conditions to protect the economy. However, with their COVID-era stimulus measures still very much in force and inflation at worrying levels, the Fed instead embarked on what is forecast to be an extended tightening process by raising rates a quarter of a point in March.

The tumultuous macro backdrop led to considerable volatility and a wide dispersion of returns across sectors. The markets sold off sharply in January and February. Growth indices were particularly hard hit, as investors began to price in the impact of higher rates on these long-duration assets. March, however, brought a wave of buying, spurring a partial recovery in growth and pushing value indices almost to break-even for the quarter. As is to be expected in turbulent times, larger capitalization stocks generally performed better than smaller ones. Among sectors, Energy was the standout with soaring oil prices driving shares across the capitalization spectrum up more than 35%. Conversely, investors worried about the impact of inflation, rising rates, and general uncertainty on consumer spending and corporate margins, which drove shares of Consumer Discretionary companies down close to 10% for the quarter.

Portfolio Performance & Developments

Amidst another tumultuous quarter, Cooke & Bieler's Large Cap Value Strategy outperformed the Russell 1000® Value Index, posting 0.29% gross of fees (0.13% net of fees) against a -0.74% return for the benchmark. Stock selection effect accounted for more than all of the portfolio's outperformance, while sector allocation effect was a partial negative offset. Selection effect was especially strong in Financials, with insurance companies such as Alleghany, Arch Capital, and Allstate being the most notable contributors. Communication Services holdings also benefited relative results significantly, particularly Activision Blizzard and Omnicom Group. Utilities, Materials, and Health Care contributed modestly as well. Conversely, Industrials, Consumer Staples, and Consumer Discretionary holdings detracted from results, particularly AerCap, Unilever, and Whirlpool.

Five Largest Contributors/Detractors

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
Leidos	2.5	21.9	54
Activision Blizzard	2.4	20.4	51
Alleghany	1.8	26.9	49
Williams Companies	1.8	30.0	47
Berkshire Hathaway	2.5	18.0	43

	Avg Weight (%)	Total Return (%)	Contrib. to Return (bps)
AerCap	3.0	-23.1	-66
Stanley Black & Decker	2.1	-25.5	-60
Whirlpool	1.8	-25.7	-49
IAA	1.9	-24.4	-47
Arrow Electronics	3.6	-11.6	-42

Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Large Cap Value institutional portfolio's gross of fees return relative to the Russell 1000® Value Index. The holdings identified do not represent all of the securities purchased, sold, or recommended for Cooke & Bieler's Large Cap 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

Leidos (LDOS), a leading provider of information technology and other services to the government, was the largest contributor. LDOS recovered from prior underperformance as investors shifted their views on defense spending in light of the Russia-Ukraine conflict, in addition to higher civilian budgets.

Activision Blizzard (ATVI), a video game developer and publisher, was the second-largest contributor. ATVI traded up on Microsoft's announcement that it was acquiring ATVI in an all-cash deal at a premium to its pre-announcement share price. Regardless of deal closure, ATVI benefits from video games becoming increasingly mainstream and its franchises remain healthy.

Alleghany (Y), a reinsurance and specialty insurer, was the third-largest contributor. The company announced it was being acquired by Berkshire Hathaway at a 25% premium to both its book value and its pre-announcement stock price.

Large Cap Value Equity

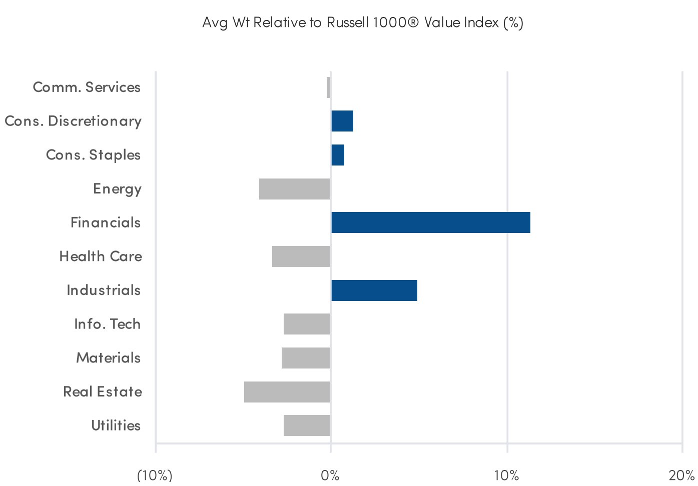
Largest Detractors

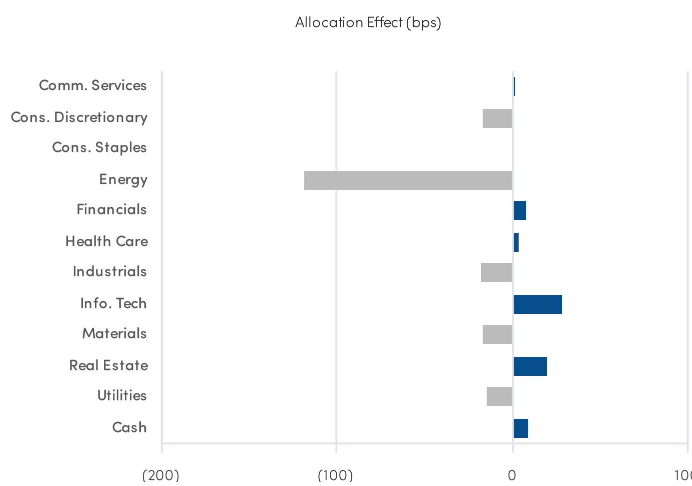
AerCap (AER), the largest independent aircraft lessor, was the largest detractor. Investors reacted negatively to the company's exposure to Russian airlines. In response to sanctions, Russian airlines have breached their contracts for aircraft and engines belonging to AER worth about $2.5B. While the fate of these planes and resulting insurance claims is hard to assess, the company's overall exposure should prove to be manageable, and we believe AER remains well positioned longer term.

Stanley Black & Decker (SWK), an industrial and household tool manufacturer, was the second-largest detractor. SWK suffered from investor concerns over both the impact of inflation on its unit economics and the effects of higher interest rates on overall building and remodeling activity.

Whirlpool (WHR), a global manufacturer and marketer of home appliances, was the third-largest detractor. WHR has posted impressive margin performance and earnings growth as demand for home appliances remains robust. However, investor concerns over input cost inflation, a potential recession, and the impact of rising interest rates on the housing market have weighed on the stock price. While the company's strong current fundamentals are likely to recede, its valuation is very attractive relative to our estimate of its earnings power.

Sector Positioning





Source: FactSet
Past performance is not indicative of future results. The performance attribution is an analysis of a representative Large Cap Value institutional portfolio's gross of fees sector return relative to the Russell 1000® Value Index. Please see additional performance disclosures at the end of this document.

Allocation effect detracted from relative performance in the first quarter of the year, with mixed results across sectors. An underweight to Energy – by far the standout performer in the benchmark with a return of nearly 40% – was the primary driver. An overweight to the pro-cyclical Industrials and Consumer Discretionary sectors as well as an underweight to Materials and Utilities posed more modest headwinds. The portfolio's underweight to the more economically sensitive Real Estate and Information Technology sectors generated a partial positive offset.

Initiations

Carmax (KMX) is an independent used car retailer that operates through both brick & mortar and online channels with over $20 billion in annual sales. KMX sells vehicles through direct retail and wholesale auction channels, supporting its retail business with ancillary products such as financing, warranty, and service plans. The company's scale enables it to make more data-driven decisions on its inventory to avoid significant depreciation. We expect KMX to gain share in the fragmented used car market due to its low-friction customer experience, increasing use of technology, and willingness to leverage different business segments to achieve strong results for the company as a whole.

Eliminations

Reliance Steel (RS) and **Schlumberger (SLB)** reached their price targets and were eliminated.

COOKE & BIELER

Q1 2022

Large Cap Value Equity

Outlook

The extremely unsettled macro backdrop is creating challenges both for managements forced to reevaluate their supply chain and pricing strategies and investors struggling to untangle the complicated interactions between inflation, monetary policy, and geopolitical tension. So far, the market seems to be pricing in a severe and long lasting consumer recession – particularly among smaller cap names – and a lasting boom in oil prices. We take these potential outcomes seriously and have re-underwritten consumer exposed portfolio holdings and re-examined our underweight to Energy. The portfolio remains overweighted the economically sensitive Consumer Discretionary and Industrials sectors, which may present a short term headwind to performance. Over a full cycle, however, we believe the portfolio's higher quality holdings – businesses with more pricing power and more favorable demand environments – will generate attractive returns, particularly given their current valuations. Conversely, we believe the run up in energy prices is, if anything, likely to undermine the long term attractiveness of these businesses as adding geopolitical risks to existing climate pressures will only speed the move away from fossil fuels. Short term relative performance is impossible to manage, and the portfolio's decidedly out of consensus positioning may not work in the short term - however, our experience is that patience and steadfast focus is generally rewarded over time.

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

Additional Cooke & Bieler Large Cap Value Performance Disclosures