

# Large Cap Value Select

A CONCENTRATED, HIGH CONVICTION STRATEGY | QUARTERLY UPDATE AS OF SEPTEMBER 30, 2020



## Investment Objective

Long-term total return = Russell 1000 Value index plus 200 bps to 400 bps

## Strategy Highlights

River Road's Large Cap Value (LCV) Select Strategy is a concentrated, high conviction value strategy comprised of companies that exhibit attractive business models, shareholder-oriented management, and financial strength.

The Strategy's investment universe formally consists of all North American listed equity securities with market capitalizations greater than \$2 B at the time of initial purchase.

## Portfolio Managers



**Daniel R. Johnson, CFA, CPA**

14 years of experience;  
managed Portfolio since inception

University of Kentucky, BS  
University of Kentucky, Macc



**Matt W. Moran, CFA**

20 years of experience;  
managed Portfolio since inception

Bradley University, BS  
University of Chicago, MBA

## Performance Summary



	Q3 2020	YTD	1 YR	3 YR	5 YR	Inception
LCV Select Composite - Gross	7.26%	-9.88%	-3.35%	3.85%	9.29%	7.53%
LCV Select Composite - Net	7.19%	-10.07%	-3.62%	3.34%	8.69%	6.92%
Russell 1000 Value	5.59%	-11.58%	-5.03%	2.63%	7.66%	5.23%
Out / Underperformance	+1.67%	+1.70%	+1.68%	+1.22%	+1.63%	+2.30%

Performance is shown gross and net of fees. Inception date: November 1, 2014. Out/underperformance compares gross performance and the index. Source: River Road Asset Management LLC and Russell Investment Group. Past performance is no guarantee of future results. Please see appendix for the disclosure presentation.

## Portfolio Review

**The robust recovery in stocks that began on March 24 remained intact during Q3 as explosive returns in July and August were partly offset by a pullback in September.** Early in the quarter, returns were fueled by a combination of record central bank liquidity and fiscal stimulus, which provided critical catalysts to jumpstart a recovery and end what could be the shortest recession in history. According to Ned Davis Research, **the five-month period ending in August was the best for the S&P 500 since 1938.**

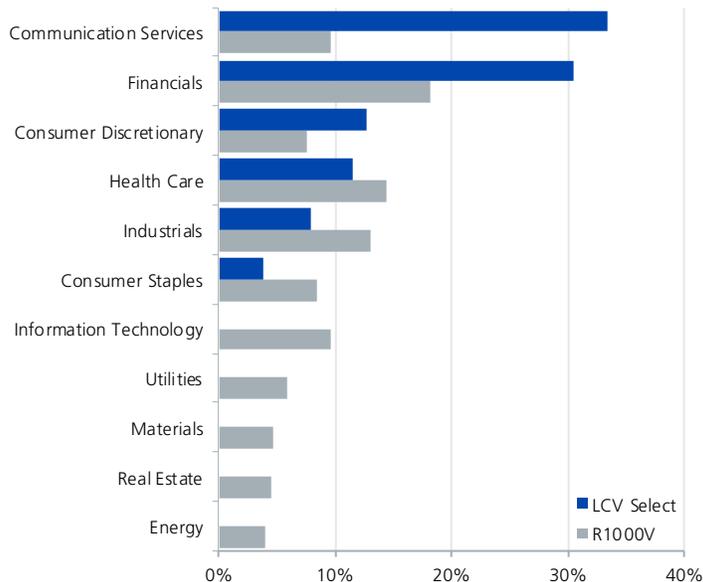
**Despite the September pullback, gains for the quarter still skewed heavily to large cap and growth stocks.** For Q3, the S&P 500 and Russell 1000 indices returned **+8.93%** and **+9.47%**, respectively, versus **+4.93%** for the Russell 2000. It was the best Q3 for the tech-heavy S&P 500 since 2010. Additionally, the Russell 1000 Growth index returned **+13.22%** for Q3 versus just **+5.59%** for the Russell 1000 Value. Year to date, the gap between growth and value is astonishing, with an unprecedented **+3,591 bps** difference in returns between the Russell 1000 Growth (**+24.33%**) and Russell 1000 Value (**-11.58%**) indices.

The top contributing holding in Q3 was **Berkshire Hathaway Inc. (Cl B) (BRK.B)**, a collection of diverse businesses with large interests in insurance, railroads, utilities, etc. BRK.B's well run and disciplined insurance operations have generated the float (cash) for Warren Buffett to deploy, **creating what we believe is one of the world's greatest compounding machines** (+20.3% stock price from 1965 to 2019 versus +10.0% for the S&P 500). BRK.B targets businesses with **sustainable competitive advantages** and **solid balance sheets** (\$137 B in cash; 32% of market cap) that are **run by proven owner/operators**. Both Buffett and Vice Chairman Charlie Munger have the vast majority of their net worth in Berkshire Hathaway stock. **As the least Wall Street-covered large cap stock in the S&P 500**, sometimes BRK.B's stock price does not get the attention it deserves. After being ridiculed by day trader Dave Portnoy this summer, **the stock's incredible value was too hard to ignore** when the company's largest public investment, Apple Inc., increased almost +45% in the third quarter alone. At Apple's quarter-end price, **BRK.B's position in the stock represented 26% of its market cap**. Although the stock performed well this quarter, we think the market is still not appropriately valuing the company's other public and private holdings, railroad, insurance operations, etc.

The largest negative contributing holding in Q3 was **Huntington Ingalls Industries Inc. (HII)**, American's largest shipbuilder and a provider of professional services to partners in government and industry. **Leading defense companies like HII seem well positioned in a global economy suffering from negative COVID-19 aftershocks** with their primary customer, the federal government, able to print more money to fund a consistently growing defense budget (as well as funding HII's research and development budget). The company benefits from **decades-long revenue visibility** and the lack of alternative suppliers and shipyards. Investor sentiment toward defense names tends to decline before presidential elections. However, there is no correlation between the party in power and defense budgets/defense stocks' performance. **The timing of HII's guidance reduction added fuel to the selling fire.** Investors deserted the stock after management reset shipbuilding margin expectations for 2021 from previous guidance of 9% to 7%-8%. COVID-19-related workforce interruptions contributed to the reduction.

In summary, **the markets are rich, uncertainty is high**, and we expect elevated volatility. Balancing value, quality, and financial strength has become increasingly challenging. Despite strong absolute and relative performance in the Strategy, we believe the Portfolio remains attractive based on valuation. According to FactSet, the Portfolio's valuation (as measured by EV/EBITDA) is **9.7x** versus **12.4x** for the Russell 1000 Value benchmark and **16.4x** for Russell 1000. While the Portfolio's quality, as measured by five-year average return on equity, dipped slightly below the benchmark in Q3, we have maintained a financially strong Portfolio with a net leverage ratio, of **1.8x** versus **2.5x** for the benchmark. We believe the Portfolio is built for a market with elevated volatility.

## Sector Weightings



## Portfolio Contribution

Top Contributors		Avg Wgt	Contrib
BRK.B	Berkshire Hathaway Inc. (CI B)	9.37%	+1.65%
PGR	Progressive Corp.	6.14%	+1.22%
NTDOY	Nintendo Co. Ltd. Unsponsored ADR	4.40%	+1.18%
LBRDK	Liberty Broadband Corp. (CI C)	7.64%	+1.13%
CMCSA	Comcast Corp. (CI A)	6.37%	+1.11%

## Bottom Contributors

HII	Huntington Ingalls Industries Inc.	3.70%	-0.74%
MSGE	Madison Square Garden Entertainment Corp. (CI A)	4.66%	-0.50%
MPC	Marathon Petroleum Corp.	2.40%	-0.36%
GD	General Dynamics Corp.	3.64%	-0.31%
LSXMK	Liberty Media Corp. Series C Liberty SiriusXM	4.33%	-0.29%

GICS sector and market cap breakdowns reflect percent of equity; stocks without a reported sector or market cap (e.g. corporate reorganizations, mergers, acquisitions, dissolutions) are not presented. <sup>1</sup>EBITDA exclude banks, thrifts, and insurers. <sup>2</sup>Excludes negative earnings. <sup>3</sup>Risk characteristics based on trailing 60 month gross of fee composite performance. <sup>4</sup>Average calendar year turnover. Dollar turnover, the lesser of purchases or sales as a percentage of the average market value, is presented as an average of portfolios in the Composite. Source: River Road Asset Management LLC, FactSet Research Systems Inc., and Russell Investment Group.

Portfolio contribution calculated for the Q3 2020 period. For the purpose of assessing top and bottom contributors, the contribution of child securities is aggregated with that of the parent for corporate actions that occurred during the most recent calendar quarter. The holdings identified do not represent all of the securities purchased, sold, or recommended. To receive information regarding the methodology for calculating the top/bottom contributors or a list showing every holding's contribution to the overall Composite and/or representative portfolio performance contact RRAMCompliance@riverroadam.com. Past performance is no guarantee of future results.

Representative Portfolios: Unless otherwise noted as Composite, the information presented is based on a representative portfolio. If no single representative portfolio is available to represent the Strategy since inception, different representative portfolios and/or the composite are used for different periods to create a continuous representative portfolio. The representative portfolio is selected by the firm as a representative account that is deemed to best represent this management style using a pre-defined, objective set of criteria. All representative portfolio data is shown as supplemental information to the Composite presentation. Each client portfolio is individually managed and may vary from the information shown for the representative portfolio.

River Road Asset Management, LLC ("RRAM") is a registered investment adviser formed in April 2005 and is majority owned by Affiliated Managers Group, Inc. Registration of an investment adviser does not imply a certain level of skill or training. This presentation may be presented by an employee of Affiliated Managers Group, Inc., AMG Funds, or another AMG entity, which are affiliates of RRAM. RRAM claims compliance with the Global Investment Performance Standards (GIPS®). The firm maintains a complete list and description of Composites and a presentation that complies with the requirements of the GIPS® standards, which is available upon request by contacting RRAMCompliance@riverroadam.com.

The Large Cap Value Select Composite contains fully discretionary accounts that seek long-term capital appreciation by investing primarily in equity securities that trade at a discount to our valuation as determined using RRAM's proprietary Absolute Value® approach. The composite may also be invested in Real Estate Investment Trusts (REITs), publicly traded partnerships, investment companies, convertible securities, and foreign stocks. Prior to September 30, 2020, the Composite was known as the Select Value Composite. The official benchmark for the Composite is the Russell 1000 Value Index. The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 companies that are considered more value oriented relative to the overall market as defined by Russell's leading style methodology. The Russell 1000 Value Index is constructed to provide a comprehensive and unbiased barometer for the large-cap value segment. The Index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect value characteristics. All other indices are shown for additional information only. The U.S. dollar is the currency used to express performance and includes the reinvestment of income. Composite performance is presented gross of foreign withholding taxes on dividends, interest income, and capital gains. All Composite performance is after the deduction of trading costs. Net of fee performance is calculated using actual management fees. For periods including non-fee paying accounts, net was calculated for those accounts by applying the highest fee schedule effective at that time. Unless otherwise noted, performance provided for periods greater than one year is annualized.

The information provided in this report should not be considered a recommendation to purchase or sell any particular security. There is no assurance that any securities discussed herein will remain in our portfolio at the time you receive this report or that securities sold have not been repurchased. Characteristics and sector weightings of our portfolio are shown and may not be indicative of this strategy's current or future investments. It should not be assumed that any of the holdings discussed herein were or will be profitable or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein. This information is shown as supplemental information only and complements the full disclosure presentation.

Sector, Industry Group, Industry, or Sub-industry group levels are determined at the beginning of each quarter according to the Global Industry Classification Standard ("GICS"), developed and exclusively owned by MSCI Inc. ("MSCI") and Standard & Poor's Financial Services LLC ("S&P"), unless otherwise stated that they have been reclassified or classified by RRAM. Reclassifications/classifications by RRAM are not supported by S&P or MSCI. All GICS data is provided "As Is" with no warranties. RRAM may classify securities that are not automatically classified by MSCI and S&P.

Portfolio and index characteristics such as EV/EBITDA are based on companies' most recent filings as of this report date (values for many companies may be as of the prior period). Most company share-related characteristics exclude outliers. Outlier exclusion methods include interquartile and inverse interquartile; the universe for determining outliers is the Russell 3000. For more information, please contact RRAM. Unless otherwise noted, share-related characteristics are provided by FactSet.

© Copyright: All rights reserved; 2020, River Road Asset Management, LLC.

## Characteristics

	LCV Select	R1000V
Number of Holdings	22	850
EV / EBITDA <sup>1</sup>	9.7	12.4
Price / Earnings <sup>2</sup>	18.2	20.0
Price / Book	1.94	2.14
Price / Cash Flow	11.7	15.8
ROE (5 YR Avg)	14.7	16.0
EPS Growth (5 YR)	14.8	8.8
LT Growth Estimate	9.9	6.7
Annualized Standard Deviation <sup>3</sup>	16.74	15.37
Jensen Alpha <sup>3</sup>	1.38	
Beta <sup>3</sup>	1.04	
Dollar Turnover (3 YR Avg) <sup>4</sup>	69.84%	

## Market Capitalization Breakdown

	LCV Select	R1000V
Wtd Median Market Cap	\$39.72 B	\$65.13 B
Wtd Avg Market Cap	\$146.67 B	\$122.19 B
Large/Mega: > \$25 B	61.7%	72.8%
Mid: \$5 B - \$25 B	28.0%	23.2%
Micro/Small: < \$5 B	10.3%	3.9%

## Top 10 Portfolio Holdings

Symbol	Company	% of Port
BRK.B	Berkshire Hathaway Inc. (CI B)	9.72%
LBRDK	Liberty Broadband Corp. (CI C)	7.92%
CMCSA	Comcast Corp. (CI A)	6.75%
LSXMK	Liberty Media Corp. Series C Liberty SiriusXM	5.73%
DLTR	Dollar Tree Inc.	5.13%
FNF	Fidelity National Financial Inc. - FNF Group	4.99%
PGR	Progressive Corp.	4.73%
MSGE	Madison Square Garden Entertainment Corp. (CI A)	4.38%
AFG	American Financial Group Inc.	4.26%
PINC	Premier Inc. (CI A)	4.02%

