1Q 2026
Value*Plus* Portfolio Review

During the recently ended quarter, net of fees, the ValuePlus composite out-performed the Morningstar Large Cap Value by 194 basis points and out-performed the S&P 500 Value by 427 basis points. The 1-year net of fee return on the composite was 11.5%; the 5-year net of fee return on the composite was 11.1%; and the 10-year net of fee return on the composite was 11.3%.

For several years now, more and more stocks suffer from the crowding out effect which represents only one side of the indexation coin. The majority of the market's attention has gone to the largest companies in the index, Nvidia, Apple, etc. The other side of this concentration effect, however, are the rising number of companies and sectors that have become under-represented in the index. The mechanical construct based on free float market-capitalization that allocates increasingly larger weights to securities that have already appreciated means that indices are susceptible to shocks under most adverse scenarios; they are not set up to perform with desirable return characteristics in anything but a narrow subset of conditions.

This is precisely what took place in the first quarter. Since indexes are primarily formulaic, they do not consider the importance of various sectors on the economy. They tout Nvidia and the semiconductor industry in general but fail to appreciate that semiconductor manufacturing requires certain gases like helium that are provided by companies like Air Products. They clamor for the benefits of AI and hyper-scalers but fail to appreciate that massive data loads need to flow through established networks owned by AT&T and Verizon. They bemoan the volatility of commodities and interest rates but fail to appreciate companies like the CME that offer protection against such erratic prices. Most obviously, they hype low prices and instantaneous delivery but fail to incorporate the costs of manufacturing and distribution, driven first and foremost by the price of oil, gasoline, and diesel.

In what might appear to be counter-intuitive, indexation is one of the value investor's best friends. As Active Value investors, we want to own companies necessary for the functioning of the economy yet which are generally ignored by quantitively-derived markets. The value of such companies may not be appreciated in the short-term but tends to be recognized over time.

It just so happens that Value*Plus* is laden with companies like those mentioned above. It also happens that the first quarter demonstrated what happens when the significance of previously ignored companies becomes recognized.

During the quarter, Value*Plus* outperformed its benchmarks *(net-of-fees)* due to stock selection as well as sector allocation. Importantly, we were underweight communications, an area that warrants additional mention. As discussed in our last portfolio review, until mid-year last year, Value*Plus* was generally "equal-weight" our primary benchmark in communications. Yet, suddenly, due to index rebalancing, Value*Plus* found itself significantly "under-weight". What was the cause of this change since we had not drastically altered our position? Our benchmark had decided that both Alphabet and Meta should become the largest weights in the sector, and by no small measure at that. Alphabet became

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the largest position in the entire index while Meta also figured prominently among the ten largest index positions, not to mention its size in the communications sector. That is how Value*Plus* became "under-weight." In response to such a sudden change, passive or closet value managers would have likely purchased those two behemoths. What we did instead was to add to our exposure to traditional telecommunications positions by increasing our weight in AT&T and by initiating a position in Verizon. A few months later, the value of these two companies continues to be under-appreciated by the market despite the privileged positions they enjoy in the entire AI buildout. The primary distinction AT&T and Verizon possess is that they have already completed much of their capital spending whereas Alphabet (Google) and Meta are just beginning theirs. Our personal preference is to invest in companies that have excess capital with which to reward us as shareholders in the form of attractive dividends. Communications was the largest source of relative out-performance during the quarter.

That energy exposure can be beneficial to one's financial wellbeing has recently become clear. Value*Plus* has been overweight energy for a number of years as many of the operators have demonstrated capital discipline, not entirely unlike AT&T and Verizon in that respect. With adequate commodity prices and limited capital-raising abilities, companies have been forced to spend within their means, in stark contrast to the prior decade. Yet despite constructive industry fundamentals, once again, indexation resulted in companies like Exxon Mobil and Chevron being mostly ignored. We delight in investing where prices are not reflective of improving fundamentals. We did not anticipate the Iran war by any means yet the recent spike in oil prices brings to light the earnings potential of the energy complex under a better-than-adequate environment. We invested during a challenging environment with our base case being capital discipline. What we're getting in return is a warranted premium on anything but a benign geo-political climate. It has been decades since any energy company figured within the largest index constituents. We would not be surprised to see more than one among them in the not-too-distant future. Of course, that would imply that a few technology companies might drop off the list, a prospect we also see as quite likely.

Healthcare was the third largest area of relative out-performance and consumer discretionary was the fourth. From a sector level standpoint, they both benefited from similar dynamics as telecommunications and energy.

Despite out-performing from an overall stock selection standpoint, there were a few meaningful detractors to overall performance in the period. Graphic Packaging, Diageo, 3M, IBM, and Nike all declined in the period. Graphic Packaging falls within the packaging sector which was weak overall. In addition, the company's end markets have been challenged and changes in management are creating friction between the board and activist investors. Due to the confluence of factors affecting the company and placing additional weight on company specific concerns, we are unlikely to increase our position. Should the stock remain depressed while fundamentals improve, we will revisit this stance. Diageo has declined for similar reasons: the environment has been weak and some of the company's products are experiencing lower demand. As with Graphic Packaging, Diageo has also experienced recent management changes. Since the reasons for its stock weakness are quite similar to those of Graphic Packaging, albeit in a very different industry, we likewise do not plan to increase our position unless and until the company's fundamentals improve. Lastly, Nike suffers from similar concerns which we think will not prove to be permanent. Our error has not so much arisen from being interested in the company based on the combination of valuation attraction (on normal earnings power) and prospective fundamental improvement, both of which remain in place. Our error has come from gradually adding to our position prior to seeing more meaningful signs of a turn in all segments.

3M and IBM fall into an altogether different category, the category of companies having performed well and perhaps because of having done so, experience some level of "profit-taking". 3M continues to improve its business, its competitiveness and its return to shareholders. Yet because of its economic sensitivity, shares have declined noticeably. Were 3M not an already fairly large position, we would be adding to our position at current levels. Similarly, IBM's fundamental improvements over the last few years has been commendable. As such, shares were recently valued richly. We had been trimming our position due to valuation concerns but wanted to maintain exposure based on the company's

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significant optionality in some of its businesses. At today's more reasonable price levels, we are pleased with our position and would also consider increasing.

Some of the largest contributors during the quarter were the prior quarter's detractors. Kontoor Brands, AT&T, Verizon, the CME and Hasbro were among the largest individual contributors. Kontoor, AT&T and Verizon remain incredibly attractively valued with good to improving fundamentals. The CME is more richly valued, a valuation that is nevertheless warranted due to its attractive margin profile and which offers desirable diversification in a financial sector fraught with risks.

During the quarter we eliminated two positions: Genuine Parts and Royal Philips. While we believe Genuine Parts was a successful investment by most measures, we are disappointed at the gradual change in corporate governance and objectives. GPC, as the company was also known, had traditionally been a compounder and was considered among the best operators in its respective industries. A gradual changing of the guard nevertheless resulted in a deterioration in capital allocation priorities and competitive positioning. Recently, the company announced it would break itself in two. We have stepped to the sidelines and may revisit once the split is completed. Royal Philips was also eliminated following the increase in its stock due to improved fundamentals. We have owned Royal Philips twice over the last few years with both instances being profitable. Should shares decline once again on what we would view to be less-than-permanent pretexts, we wouldn't hesitate to be buyers once again.

Value*Plus'* portfolio positioning—in sectors generally neglected by consensus—has demonstrated its benefits in benign as well as in averse environments. If one thing remains constant, it is that each environment presents us with opportunities to purchase companies that many are fearful of owning. We look forward to reporting to you in another three months.

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