

Baird Recommended Equity Portfolio

Quarterly report for 1Q22

The Recommended Portfolio fell 9.6% (gross of fees) during the first quarter, below the S&P 500's total return of -4.6% (includes dividends).

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Portfolio Changes

Across the first quarter, we sold full positions in **PayPal** (PYPL), **NextEra** (NEE), **Ecolab** (ECL), **Meta Platforms** (FB), **Nike** (NKE), **Starbucks** (SBUX), **Adobe Systems** (ADBE), and **D.R. Horton** (DHI). Many of these moves were fueled by valuation concerns as we head into a set of conditions—Fed hiking rates, elevated inflation—that has historically been associated with multiple contraction. Beyond valuation, many of our sales were fueled by a lack of meaningful upside catalysts, stock-specific issues, and a rapidly shifting macro environment. In addition to the outright sells mentioned above, we trimmed positions in **Rockwell Automation** (ROK) and **Apple** (AAPL) near quarter-end.

We used the proceeds from these moves to fund a handful of new positions. We bought (and later added to) both **Discovery** (DISCK), which is poised to become a streaming giant following its merger with WarnerMedia, and **Paychex** (PAYX), a provider of HR services that is set to benefit from the underlying strength of the labor market. We also initiated positions in **Corning** (GLW), **MetLife** (MET), **Chipotle** (CMG), **Reliance Steel** (RS), and **AmerisourceBergen** (ABC).

We bolstered positions in a few higher conviction ideas: **EOG Resources** (EOG), one of the best-positioned Energy names, **Tractor Supply Co.** (TSCO), a high-quality growth name in the consumer space, **Caterpillar** (CAT), an industrial behemoth positioned to benefit from strength in commodities and end-markets, **CostCo** (COST), a quality staple with pricing power, and **Chubb** (CB), an insurer with the potential to benefit from rising interest rates.

The above-average turnover across 1Q22 reflected both the rapidly shifting macro environment and the bifurcation of individual stock stories. As a result, we continued a marginal portfolio shift away from Growth and toward Value holdings over the course of the first quarter. We feel confident that these moves have positioned us well to benefit from higher (and more persistent) inflation, tighter monetary policy, and strong-but-decelerating economic growth in the US.

Market and Portfolio Performance

On the quarter, the S&P 500 finished -4.6%, its worst non-recession Q1 since 1977. At an asset-class level, large-cap outperformed its small- and mid-cap counterparts, while Value handily outperformed Growth. The Baird Recommended Portfolio trailed the benchmark with a total return (which includes dividends) of -9.6%.

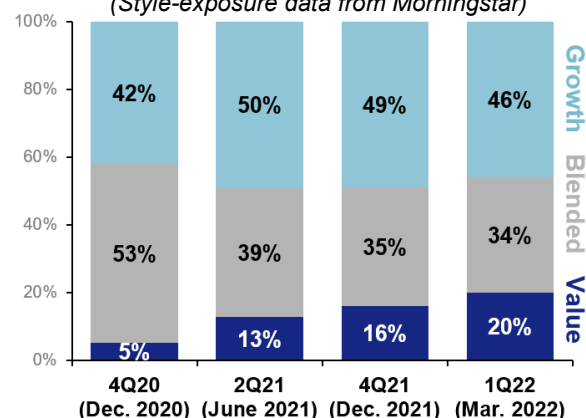
Among S&P sectors, there was Energy (+39.0%) and then there was everything else. Oil and natural gas prices skyrocketed (33.3% and 58.4%) on reopening demand, production discipline from OPEC+ and US shale, and Russia/Ukraine supply shocks. Utilities (+4.8%) were the only other sector in the black; their defensive and stable nature bolstered performance despite rising interest rates.

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Please see page 4 for important disclosures

A Shift Toward Value

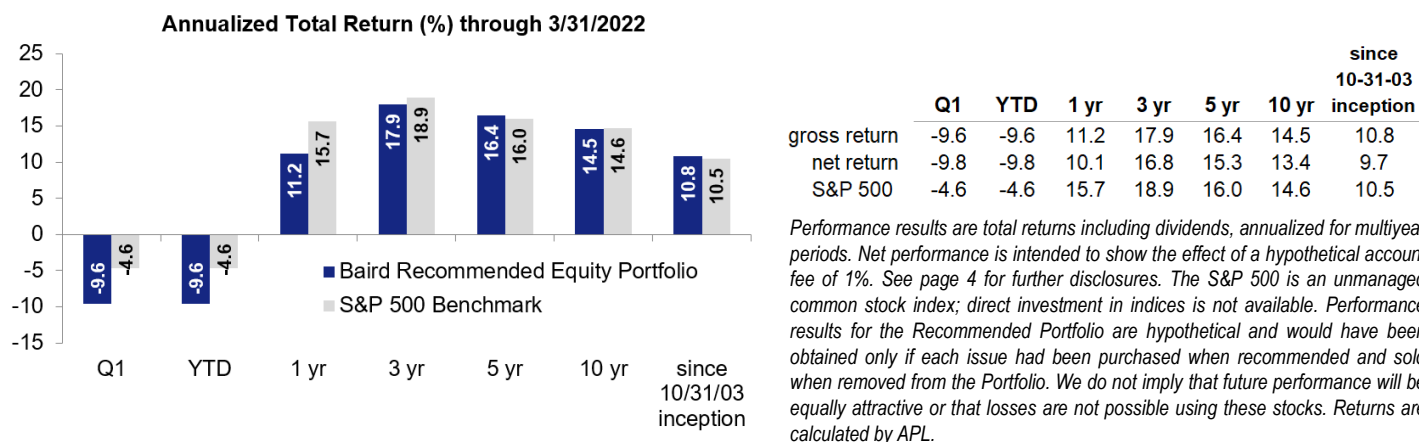
(Style-exposure data from Morningstar)



In response to a shifting macro environment, we have moved the Recommended Equity portfolio stylistically toward Value over several quarters.

Baird Recommended Equity Portfolio

On the flipside, Communication Services (-11.9%), Consumer Discretionary (-9.0%), and Technology (-6.2%) lagged. These mostly-Growth sectors underperformed amid continued supply chain issues, decelerating earnings growth, and rates-driven multiple compression. Communication Services is the only sector negative over the trailing one-year, while the S&P 500 is up 15.7% over the same period.



Market Commentary

Markets suffered a volatile 1Q22, as a combination of historic inflation, war in Ukraine, and an increasingly aggressive Federal Reserve sent both stocks and bonds lower. The S&P 500 was down -13% at its worst before rallying strongly into quarter-end. Bond markets weren't as lucky, with the US Treasury Index posting its worst quarter in over 50 years amid rapidly rising interest rates. War in Ukraine further complicates the macro picture, as many commodity prices are spiking and the Euro-area is inching toward recession. After a mostly calm 2021, volatility was elevated in Q1. On more than half of the quarter's trading days, the market closed higher or lower by 1% or more.

While Russia-Ukraine received most of the press, it was the Federal Reserve that ultimately drove markets in Q1. The S&P 500 was already off ~10% before Russia invaded Ukraine in February, as inflation came in hotter than feared and the Fed was forced to get more aggressive. Though investors knew that the Fed would begin raising rates in 2022, the speed and size of the expected hikes shifted significantly across the quarter. At year-end, markets priced three 2022 rate hike, but by March 31, they were pricing ten. The Fed hasn't raised rates in a 0.50% increment in over two decades (0.25% has been the norm), but markets now expect two such moves by July. There is a growing sense that the Fed will "tighten until something breaks."

Of course, this response isn't entirely unjustified. Inflation is at 40-year highs and looking stickier by the day (wage growth, inflation expectations, and rents are all meaningfully higher) at the same time that the domestic economy is running hot. Labor markets are extremely strong (record job openings, historically low unemployment) and broad economic growth—retail sales, manufacturing, etc.—is healthy, if often hampered by supply chain woes. Further, the US economy looks relatively well-insulated from the strife in Ukraine, (though not entirely, see: gas prices). All said, the Fed finds itself behind the curve and looking to make up ground quickly.

All of this comes together to form a macroeconomic environment unlike any in recent memory. For the first time in decades, the Energy sector is meaningfully outperforming, Big Tech/Large Growth is stumbling, and long-term interest rates are spiking (even as stocks fall). Even the question of where we are in the business cycle is up for debate. In the end, while the macro winds shift rapidly, we believe a focus on higher quality is prudent at this time. Higher interest rates and supply-side uncertainty favor operators with strong margins (and the ability to protect them), high returns on capital, and—perhaps more than usual—competent management. As our partners at Strategas have noted, high inflation and high interest rate regimes tend to see multiple contraction. Therefore, a focus on the earnings and dividend portion of total return should be a boon across the remainder of 2022.

Date: 3/31/22

BAIRD'S RECOMMENDED PORTFOLIO

Ticker	Company Name	Portfolio %	S&P %	Purchase Date	Purchase Price (\$)	3/31/22 Price (\$)	% Change (%)	52 Week High (\$)	52 Week Low (\$)	Market Cap (\$mil)	NTM Rev Growth (%)	NTM EPS Growth (%)	NTM P/E (x)	NTM EV/EBITDA (x)	Dividend Yield (%)
Communication Services		5.8%	9.4%												
GOOG	Alphabet Inc. Class C	4.4%		Multiple	502.28	2792.99	456.1	3042.00	2096.89	1,842,312	17.1	7.7	22.9	13.2	0.0
DISCK	Discovery, Inc. Class C	1.4%		Multiple	30.40	24.97	-17.9	38.16	20.86	12,701	2.9	4.2	8.9	5.2	0.0
Consumer Discretionary		10.4%	12.0%												
AMZN	Amazon.com, Inc.	3.8%		Multiple	1076.35	3259.95	202.9	3773.08	2671.45	1,658,807	15.8	-10.6	60.1	18.8	0.0
BBWI	Bath & Body Works, Inc.	1.0%		12/1/21	75.13	47.80	-36.4	82.00	45.46	11,420	3.9	5.7	10.0	7.3	1.7
CMG	Chipotle Mexican Grill, Inc.	1.0%		3/1/22	1523.35	1582.03	3.9	1958.55	1277.41	44,347	14.5	26.4	46.4	28.2	0.0
HD	Home Depot, Inc.	2.0%		Multiple	89.38	299.33	234.9	420.61	298.40	312,572	2.1	4.3	18.4	13.4	2.5
TSCO	Tractor Supply Company	2.6%		Multiple	230.81	233.37	1.1	241.54	170.82	26,172	7.8	9.2	24.3	15.3	1.6
Consumer Staples		4.7%	6.1%												
STZ	Constellation Brands, Inc. Cl A	1.7%		Multiple	196.26	230.32	17.4	258.00	207.35	43,689	7.6	14.5	19.8	15.2	1.3
COST	Costco Wholesale Corporation	3.0%		Multiple	115.60	575.85	398.1	586.32	351.63	255,231	9.7	12.6	41.8	23.4	0.5
Energy		5.3%	3.9%												
EOG	EOG Resources, Inc.	3.0%		Multiple	99.36	119.23	20.0	124.89	62.81	69,796	9.6	31.9	9.3	4.8	2.5
PXD	Pioneer Natural Resources	2.3%		Multiple	117.44	250.03	112.9	260.00	133.73	60,728	28.6	54.8	9.7	5.5	4.2
Financials		15.5%	11.1%												
BAC	Bank of America Corp	2.8%		Multiple	30.62	41.22	34.6	50.11	36.51	332,637	6.0	-2.6	12.1	nmf	2.0
BLK	BlackRock, Inc.	2.3%		Multiple	200.93	764.17	280.3	973.16	660.15	116,186	9.6	7.6	17.8	12.3	2.6
CB	Chubb Limited	2.4%		Multiple	169.02	213.90	26.6	218.99	155.78	91,170	5.0	16.0	14.1	11.0	1.5
MET	MetLife, Inc.	2.0%		Multiple	67.06	70.28	4.8	72.55	55.21	57,986	-2.4	-14.0	9.4	7.6	2.7
JPM	JPMorgan Chase & Co.	2.6%		Multiple	44.93	136.32	203.4	172.96	127.27	402,527	3.2	-19.3	11.8	nmf	2.9
MS	Morgan Stanley	1.4%		8/16/21	103.94	87.40	-15.9	109.73	76.25	155,686	-0.4	-3.5	11.3	nmf	3.2
SPGI	S&P Global, Inc.	2.0%		Multiple	410.58	410.18	-0.1	484.21	355.51	142,343	38.6	2.8	29.3	21.8	0.8
Healthcare		14.7%	13.6%												
ABC	AmerisourceBergen Corporation	1.5%		3/16/22	151.39	154.71	2.2	156.94	111.34	32,356	7.9	11.6	13.8	9.1	1.2
DHR	Danaher Corporation	2.3%		Multiple	80.56	293.33	264.1	333.96	224.14	209,834	4.9	4.4	27.7	20.2	0.3
EW	Edwards Lifesciences Corp.	2.2%		Multiple	82.95	117.72	41.9	131.73	83.12	73,141	10.6	14.2	44.8	34.5	0.0
HCA	HCA Healthcare Inc	2.1%		Multiple	211.50	250.62	18.5	272.26	185.21	75,692	4.4	8.5	12.9	8.6	0.9
IQV	IQVIA Holdings Inc	1.8%		Multiple	102.01	231.21	126.7	285.61	191.84	44,141	7.9	13.1	22.0	15.7	0.0
TMO	Thermo Fisher Scientific Inc.	1.8%		Multiple	111.14	590.65	431.4	672.34	438.72	231,057	6.9	-6.1	25.7	21.4	0.2
VEEV	Veeva Systems Inc Class A	1.1%		10/4/21	288.17	212.46	-26.3	343.96	166.48	32,669	17.0	9.2	51.5	33.9	0.0
ZTS	Zoetis, Inc. Class A	1.9%		Multiple	117.69	188.59	60.2	249.27	155.41	88,977	8.4	10.6	35.4	24.2	0.7
Industrials		10.6%	7.9%												
CAT	Caterpillar Inc.	2.4%		Multiple	226.75	222.82	-1.7	246.69	179.67	119,407	10.3	14.6	17.4	11.2	2.0
GNRC	Generac Holdings Inc.	2.0%		Multiple	121.93	297.26	143.8	524.31	251.74	18,960	27.5	20.0	24.5	16.2	0.0
OSK	Oshkosh Corp	1.4%		1/15/21	94.01	100.65	7.1	137.47	95.79	6,704	8.1	18.5	14.4	8.4	1.5
ROK	Rockwell Automation, Inc.	2.0%		Multiple	215.65	280.03	29.9	354.99	250.65	32,538	11.3	12.7	24.6	18.7	1.6
UNP	Union Pacific Corporation	2.8%		Multiple	199.45	273.21	37.0	278.94	195.68	171,682	8.1	15.2	22.9	15.5	1.7
Information Technology		28.5%	28.0%												
APH	Amphenol Corporation Cl A	1.5%		11/17/21	84.98	75.35	-11.3	88.45	64.13	45,130	8.2	10.7	26.7	16.6	1.1
AAPL	Apple Inc.	5.3%		Multiple	3.72	174.61	4593.8	182.94	122.25	2,849,538	7.0	8.2	27.4	20.7	0.5
GLW	Corning Inc	1.3%		2/1/22	42.04	36.91	-12.2	46.82	33.93	31,213	6.5	13.5	15.2	8.4	2.9
KEYS	Keysight Technologies Inc	1.4%		Multiple	62.08	157.97	154.5	209.08	134.65	28,747	6.4	10.5	21.8	16.9	0.0
MA	Mastercard Incorporated Cl A	2.0%		Multiple	16.75	357.38	2033.6	401.50	305.61	349,331	18.0	23.2	32.7	24.8	0.5
MSFT	Microsoft Corporation	6.1%		Multiple	92.66	308.31	232.7	349.67	238.05	2,311,359	15.1	15.5	29.6	20.2	0.8
NVDA	NVIDIA Corporation	4.3%		Multiple	75.79	272.86	260.0	346.47	134.59	684,879	27.3	26.0	46.7	36.2	0.1
PAYX	Paychex, Inc.	2.1%		Multiple	120.06	136.47	13.7	140.67	92.74	49,233	7.8	9.9	34.3	22.6	1.9
QCOM	Qualcomm Inc.	1.6%		9/2/21	146.69	152.82	4.2	193.58	122.17	172,228	15.9	19.8	12.6	9.6	1.8
CRM	salesforce.com, inc.	1.6%		Multiple	145.43	212.32	46.0	311.75	184.44	210,197	20.5	1.8	43.8	20.4	0.0
NOW	ServiceNow, Inc.	1.3%		10/18/21	663.18	556.89	-16.0	707.60	448.27	111,378	25.3	25.0	71.0	42.2	0.0
Materials		0.9%	2.6%												
RS	Reliance Steel & Aluminum Co.	0.9%		3/1/22	190.87	183.35	-3.9	198.44	135.46	11,314	0.0	-8.0	9.0	5.5	1.9
Real Estate		0.0%	2.7%												
Utilities		0.0%	2.7%												
Cash		2.9%													

Earnings and revenue growth estimates are Factset Consensus estimates. P/E is price/earnings ratio; EV/EBITDA is the Enterprise Value/Earnings Before Interest, Taxes, Depreciation, and Amortization ratio

Dividend yield equals indicated annual dividend (most recently paid common dividend annualized for the next 12 months) divided by current stock price. NTM = Next 12 Months; nmf = not meaningful

Appendix—Important Disclosures

S&P 500 and Baird Recommended Portfolio performance calculations are total returns, which include the impact of dividends. Future dividends are not guaranteed and can be lowered or suspended by companies.

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