

# Baird Recommended Equity Portfolio

Quarterly report for 2Q22

The Recommended Portfolio fell 17.7% (gross of fees) during the second quarter, below the S&P 500's total return of -16.1% (includes dividends).

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## Portfolio Changes

Across the second quarter, we sold full positions in **Veeva Systems** (VEEV), **Oshkosh Corp** (OSK), **Zoetis** (ZTS), **Edwards Lifesciences** (EW), **Keysight Technologies** (KEYS), **Rockwell Automation** (ROK), **IQVIA** (IQV), **Morgan Stanley** (MS), and **Caterpillar** (CAT). Many of these moves were fueled by valuation or cyclical concerns in tandem with a Fed tightening cycle and elevated inflation, that has historically been associated with multiple contraction. This logic was also employed in our trims of **Nvidia** (NVDA) and **Amazon.com** (AMZN). Finally, we trimmed **Bank of America** (BAC), **Blackrock** (BLK), **JPMorgan Chase** (JPM), **Union Pacific** (UNP), and **Constellation Brands** (STZ) to redeploy into less cyclical names, besides position size considerations.

We used the proceeds from these moves during the quarter to fund new positions in **UnitedHealth Group** (UNH), **Merck** (MRK), **Diageo** (DEO), **Coca Cola** (KO), **Walmart** (WMT), **American Tower** (AMT), **Southwest Airlines** (LUV), **Mosaic** (MOS), **Pfizer** (PFE), **Pinnacle West** (PNW), and **Raytheon Technologies** (RTX).

The portfolio's above-average turnover year-to-date so far reflects both the rapidly shifting macro environment and our consistent shift away from Growth towards Value holdings. We feel confident that these moves position us in companies better able to handle higher and more persistent inflation, tighter monetary policy, and an economic slowdown. We also hold a higher than usual cash balance right now, reflecting this more uncertain economic time period

## Market and Portfolio Performance

For 2Q22, the S&P 500 was down 16.1%, one of its worst quarters in the last half century. Across asset classes, large-cap stocks outperformed their small- and mid-cap counterparts, while Value again outperformed Growth. International markets bested US handily in local currency terms, though much of that was eaten away by a stronger US dollar, which hit a 20-year high in Q2 as rising Treasury yields and a global flight to safety saw capital shift to the US.

Among sectors, the defensive stalwarts did their duty in a choppy market – Consumer Staples (-4.6%), Utilities (-5.1%), and Health Care (-5.9%) were all outperformers. Elsewhere, Energy (-5.2%) was again a relative leader, though fears of an impending economic slowdown sent the sector tumbling into quarter-end. On the flip side, rising rates and inflationary pressure led Consumer Discretionary, Communication Services, and Technology shares to underperform.

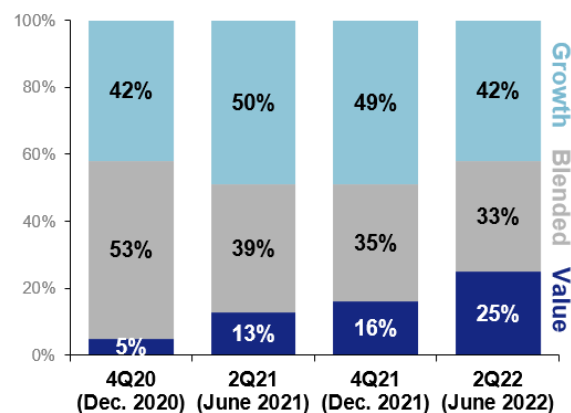
The Baird Recommended Portfolio trailed the benchmark with a Q2 total return (which includes dividends) of -17.7%. YTD, it's Energy (+31.8%) and everything else, as crude oil strength (bolstered by structurally tight supply and resilient demand) has sent the sector flying. Next best is Utilities (-0.6%), with another minor drop-off before getting to Consumer Staples (-5.6%) and

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## A Shift Toward Value

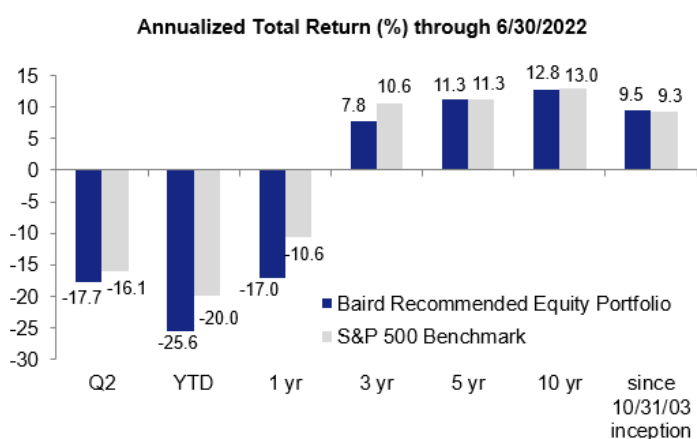
(Style-exposure data from Morningstar)



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

## Baird Recommended Equity Portfolio

Health Care (-8.3%). Bringing up the rear are Consumer Discretionary and Communication Services, which have seen above-average contraction in both price/earnings multiples and forward earnings estimates. The Baird Recommended Portfolio trails the benchmark for the full year by 5.6%, with a total return of -25.6%.



	Q2	YTD	1 yr	3 yr	5 yr	10 yr	since 10-31-03 inception
gross return	-17.7	-25.6	-17.0	7.8	11.3	12.8	9.5
net return	-17.9	-26.0	-17.8	6.7	10.2	11.7	8.4
S&P 500	-16.1	-20.0	-10.6	10.6	11.3	13.0	9.3

*Performance results are total returns including dividends, annualized for multiyear periods. Net performance is intended to show the effect of a hypothetical account fee of 1%. See page 4 for further disclosures. The S&P 500 is an unmanaged common stock index; direct investment in indices is not available. Performance results for the Recommended Portfolio are hypothetical and would have been obtained only if each issue had been purchased when recommended and sold when removed from the Portfolio. We do not imply that future performance will be equally attractive or that losses are not possible using these stocks. Returns are calculated by APL.*

## Market Commentary and Outlook

Equities continued their selloff in Q2, as persistent inflation and an increasingly hawkish Federal Reserve roiled markets. The S&P 500 closed down 16.1%, entering a bear market in June for just the second time in the last decade. Bonds fared no better, with the US Aggregate Bond index down 4.7% through June for its second worst quarter in forty years (1Q22 being the worst). The 10-year Treasury yield began Q2 at 2.32%, spiking as high as 3.48% before plummeting back to sub-3.0% by quarter-close. This led to rapid and volatile moves in other rate markets (e.g., mortgages), and contributed to a growing economic unease across the quarter.

The key problem facing the global economy remains inflation. Goods inflation has begun to soften but remains stubbornly high in some sectors as global supply chain kinks refuse to unfurl. Meanwhile, services inflation has continued to tick higher, boosted by rising wages and transportation costs, all while higher energy prices pushed the national average for a gallon of gasoline over \$5 for the first time ever. This has challenged the US consumer, which, bolstered by a white hot labor market, has displayed a willingness to spend into the teeth of inflation. It has also begun to weigh on US corporate profitability, with S&P 500 margins starting to roll over and decline (albeit off record highs).

Inflation has also remained a problem for the Federal Reserve, which is, of course, tasked with maintaining price stability. At their June meeting, the Fed raised their projections both for near-term inflation and interest rates alongside their first 0.75 percentage point rate hike since 1994. While they've maintained the stance that a "soft landing" (i.e., reducing inflation without inducing a recession) is possible, the path to that outcome is narrowing. The Fed should be able to reduce aggregate demand with higher interest rates, but they can do little to control the supply shocks driven by war in Ukraine, China's covid-zero pursuit, etc. that are reverberating throughout the global economy. The Fed also fears inflation expectations becoming unanchored, which should lead to continued hawkishness in the near-term – even as the odds of a recession grow.

Thus, despite a reasonably healthy economy today, the Fed's necessary shift in policy demands a reevaluation of the investing landscape. As we head towards a slowdown (at best) or recession (at worst), a premium should be placed on high quality operators that prioritize free cash generation, margin defense, and prudent management. Further, as per our partners at Strategas write, "In times of stress, return dispersion has historically spiked...as the dispersion of returns rises, it should bode well for active managers." We believe that economic and market volatility are likely to persist for the intermediate-term, and, while not ideal for absolute return, we see opportunity for relative outperformance. As always, a focus on strong fundamentals and quality management remains our guiding light.

Date: 6/30/22

**BAIRD'S RECOMMENDED PORTFOLIO**

Ticker	Company Name	Portfolio %	S&P %	Purchase Date	Purchase Price (\$)	6/30/22 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 (%)
<b>Communication Services</b>		5.1%	8.9%												
GOOG	Alphabet Inc. Class C	4.2%		Multiple	502.28	2187.45	335.5	3042.00	2044.16	1,437,705	15.1	8.8	17.9	10.1	0.0
WBD	Warner Bros. Discovery, Ser A	0.9%		Multiple	29.24	13.42	-54.1	31.55	12.77	32,568	60.0	-14.6	9.4	6.8	0.0
<b>Consumer Discretionary</b>		8.9%	10.5%												
AMZN	Amazon.com, Inc.	2.4%		Multiple	37.16	106.21	185.8	188.65	101.26	1,080,624	14.1	-15.7	65.0	13.0	0.0
BBWI	Bath & Body Works, Inc.	0.7%		12/1/21	75.13	26.92	-64.2	82.00	25.75	6,158	3.5	0.2	6.3	5.3	3.0
CMG	Chipotle Mexican Grill, Inc.	1.0%		3/1/22	1523.35	1307.26	-14.2	1958.55	1196.28	36,554	15.2	29.6	35.4	21.8	0.0
HD	Home Depot, Inc.	2.2%		Multiple	89.38	274.27	206.9	420.61	264.51	281,882	3.3	6.1	16.5	12.0	2.8
TSCO	Tractor Supply Company	2.6%		Multiple	230.81	193.85	-16.0	241.54	166.49	21,688	7.6	9.9	19.6	12.7	1.9
<b>Consumer Staples</b>		8.9%	7.0%												
KO	Coca-Cola Company	2.0%		Multiple	64.95	62.91	-3.1	67.20	52.28	272,717	6.7	6.9	24.8	21.6	2.8
STZ	Constellation Brands, Inc. Cl A	1.5%		Multiple	192.96	233.06	20.8	261.52	207.35	44,419	6.7	11.4	20.2	15.5	1.4
COST	Costco Wholesale Corporation	3.1%		Multiple	115.60	479.28	314.6	612.27	397.11	212,303	9.7	11.3	34.6	19.2	0.8
DEO	Diageo plc Sponsored ADR	1.0%		4/19/22	209.22	174.12	-16.8	223.14	166.24	97,796	9.7	14.6	21.2	16.3	2.3
WMT	Walmart Inc.	1.3%		5/3/22	152.99	121.58	-20.5	160.77	117.27	333,269	3.7	3.2	18.4	9.8	1.8
<b>Energy</b>		5.8%	4.4%												
EOG	EOG Resources, Inc.	3.4%		Multiple	99.36	110.44	11.2	147.99	62.81	64,686	8.6	25.6	6.9	3.8	2.7
PXD	Pioneer Natural Resources	2.4%		Multiple	117.44	223.08	90.0	288.46	133.73	53,976	20.9	33.4	7.1	4.2	7.8
<b>Financials</b>		12.8%	10.8%												
BAC	Bank of America Corp	2.0%		Multiple	29.35	31.13	6.1	50.11	30.45	250,811	6.9	3.8	8.7	nmf	2.7
BLK	BlackRock, Inc.	1.8%		Multiple	206.84	609.04	194.4	973.16	575.60	92,272	3.3	2.7	15.7	10.7	3.2
CB	Chubb Limited	2.7%		Multiple	169.02	196.58	16.3	218.99	157.19	83,293	4.6	16.0	12.2	9.5	1.7
JPM	JPMorgan Chase & Co.	2.1%		Multiple	36.32	112.61	210.0	172.96	109.30	330,741	6.0	-9.8	9.3	nmf	3.6
MET	MetLife, Inc.	2.2%		Multiple	67.06	62.79	-6.4	73.18	55.21	51,061	-0.6	-5.2	7.9	6.1	3.2
SPGI	S&P Global, Inc.	2.0%		Multiple	410.58	337.06	-17.9	484.21	311.87	116,994	24.7	4.5	24.8	19.2	1.0
<b>Healthcare</b>		15.2%	15.1%												
ABC	AmerisourceBergen Corporation	1.6%		3/16/22	151.39	141.48	-6.5	167.19	111.34	29,635	6.2	7.5	12.4	8.2	1.3
DHR	Danaher Corporation	2.5%		Multiple	80.56	253.52	214.7	333.96	233.71	184,328	4.5	4.3	24.0	18.0	0.4
HCA	HCA Healthcare Inc	1.7%		Multiple	211.50	168.06	-20.5	279.02	165.88	49,659	4.3	4.6	9.4	6.9	1.3
MRK	Merck & Co., Inc.	3.0%		Multiple	87.88	91.17	3.7	95.72	70.89	230,551	7.5	10.5	12.3	10.1	3.0
PFE	Pfizer Inc.	1.6%		6/17/22	48.51	52.43	8.1	61.71	38.93	294,179	0.1	8.7	8.6	6.7	3.1
TMO	Thermo Fisher Scientific Inc.	2.0%		Multiple	111.14	543.28	388.8	672.34	497.83	212,673	6.5	-1.3	22.8	19.3	0.2
UNH	UnitedHealth Group Incorporated	2.8%		Multiple	531.35	513.63	-3.3	553.29	383.12	481,873	9.9	14.1	21.9	15.0	1.3
<b>Industrials</b>		5.8%	7.8%												
GNRC	Generac Holdings Inc.	1.8%		Multiple	121.93	210.58	72.7	524.31	197.94	13,441	22.5	20.0	17.0	11.3	0.0
LUV	Southwest Airlines Co.	0.9%		6/1/22	45.86	36.12	-21.2	56.33	34.36	21,418	26.4	1411.7	11.5	4.4	0.0
RTX	Raytheon Technologies Corp.	1.5%		7/1/22	96.11	96.11	0.0	106.02	79.00	142,936	7.4	16.9	18.2	13.1	2.3
UNP	Union Pacific Corporation	1.6%		Multiple	192.27	213.28	10.9	278.94	195.68	133,945	8.0	13.7	17.4	12.6	2.4
<b>Information Technology</b>		25.4%	26.8%												
APH	Amphenol Corporation Class A	1.5%		11/17/21	84.98	64.38	-24.2	88.45	61.67	38,444	8.1	10.3	22.0	14.0	1.2
AAPL	Apple Inc.	5.1%		Multiple	3.72	136.72	3575.3	182.94	129.04	2,212,838	6.2	7.7	21.3	15.9	0.7
GLW	Corning Inc	1.4%		2/1/22	42.04	31.51	-25.0	43.47	30.63	26,614	6.6	12.7	12.6	7.1	3.4
MA	Mastercard Incorporated Class A	2.1%		Multiple	16.75	315.48	1783.5	399.92	303.65	306,850	17.1	22.6	27.2	21.0	0.6
MSFT	Microsoft Corporation	6.2%		Multiple	92.66	256.83	177.2	349.67	241.51	1,920,840	14.1	15.5	24.0	16.2	1.0
NVDA	NVIDIA Corporation	2.3%		Multiple	65.90	151.59	130.0	346.47	140.55	378,975	21.0	20.8	25.4	19.4	0.1
PAYX	Paychex, Inc.	2.1%		Multiple	120.06	113.87	-5.2	141.92	106.55	41,109	6.9	9.3	27.7	18.6	2.8
QCOM	Qualcomm Inc.	1.7%		9/2/21	146.69	127.74	-12.9	193.58	118.22	143,069	13.2	12.9	9.5	7.1	2.3
CRM	Salesforce, Inc.	1.6%		Multiple	145.43	165.04	13.5	311.75	154.55	164,215	19.0	9.1	32.3	15.5	0.0
NOW	ServiceNow, Inc.	1.4%		10/18/21	663.18	475.52	-28.3	707.60	406.47	95,323	25.4	26.1	57.7	35.0	0.0
<b>Materials</b>		1.9%	2.6%												
MOS	Mosaic Company	0.8%		6/1/22	62.65	47.23	-24.6	79.28	28.26	17,097	16.2	29.6	3.7	2.4	1.3
RS	Reliance Steel & Aluminum Co.	1.1%		3/1/22	190.87	169.86	-11.0	211.65	135.46	10,523	-0.1	-0.9	6.8	4.3	2.1
<b>Real Estate</b>		2.2%	2.9%												
AMT	American Tower Corporation	2.2%		Multiple	235.46	255.59	8.5	303.72	220.00	116,638	10.5	-7.5	54.9	22.7	2.2
<b>Utilities</b>		1.6%	3.1%												
PNW	Pinnacle West Capital Corp.	1.6%		6/17/22	67.80	73.12	7.8	86.87	62.78	8,263	1.4	-13.2	17.8	11.2	4.6
<b>Cash</b>		6.4%													

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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