



2020 Q2 Commentary U.S. All-Cap Value Model Portfolio July 23, 2020

BI&R's U.S. Equity All-Cap Value (ACV) model portfolio rose 20.2% last quarter versus 14.6% for the benchmark R3000 Value® index (R3000V, gross of fees). Year-to-date (YTD), our ACV model has declined 11.2% versus a 16.8% decline for the R3000V (gross of fees). While the S&P 500® appears to have declined only 3.1% YTD, this is deceiving. Twenty percent of the index consists of five mega-cap technology stocks benefitting from COVID (Microsoft +29.7%, Apple +24.9%, Amazon +49.3%, Alphabet +5.7%, and Facebook +10.6%). The median stock in the S&P 500 and R3000V has declined 11.2% and 22.4%, respectively. These median returns give a better picture of the market's true performance this year.

An investment approach or decision-maker should out-perform growth and value equity benchmarks over the long-term to demonstrate efficacy. Over my 30 ¾ years as Controlling Manager ¹ for original-EIC's All-Cap Value strategy (January 1, 1985 until September 30, 2016), returns exceeded both the S&P 500 and R3000V index (top panel below). Since then, portfolios that I have continued to manage have roughly doubled the return of the R3000V, but trailed the S&P 500. My lifetime track record since launching original-EIC in 1986 continues to exceed both indices, as shown in the bottom panel.

Barksdale Gross Returns Since 1986 ²			
	<u>Barksdale</u>	<u>R3000V</u>	<u>S&P 500</u>
<u>EIC All-Cap Value During Barksdale Tenure as "Controlling Manager" ¹</u>			
(January 1, 1986 - September 30, 2016)			
Cumulative	3030.8%	2073.9%	1980.0%
Annualized	11.9%	10.5%	10.4%
<u>Barksdale Managed Portfolios Since October 1, 2016</u>			
Q4 2016	8.0%	7.2%	3.8%
2017	17.6%	13.2%	21.8%
2018	-7.6%	-8.6%	-4.4%
2019	29.6%	26.3%	31.5%
2020 Q1	-26.1%	-27.3%	-19.6%
Q2	<u>20.2%</u>	<u>14.6%</u>	<u>20.5%</u>
YTD	-11.2%	-16.8%	-3.1%
Cumulative Since 10/1/2016	35.0%	16.7%	54.2%
Annualized	8.3%	4.2%	12.2%
<u>Barksdale Lifetime As "Controlling Manager" ¹</u>			
Cumulative	4128.1%	2436.1%	3106.8%
Annualized	11.4%	9.7%	10.5%

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COVID Versus the Fed

"Value" has become mostly irrelevant in today's market, as increased liquidity from the Fed battles reduced economic activity due to COVID. Given the high levels of corporate debt and economic uncertainty, however, quality still matters. "Quality" includes financial strength but is much broader.

A firm's ability to earn high and stable returns on capital while growing with little debt is one component of quality. Since the 2008-09 financial crisis, U.S. businesses have generated relatively high and stable returns on capital. However, real growth (i.e., growth excluding stock buy-backs and acquisitions) has been difficult due to the tepid economy. In seeking growth and quality, my post-EIC portfolios have been over-weight in technology and communications and under-weight in energy, utilities, and REITs (See BI&R 2019 Year-End Commentary). The persistent rise in stock prices within technology and communications has led to a decline in our weighting from 32.3% (third quarter of 2019) to 17.8% today.

Last quarter we expanded the concept of 'quality' to include the ability to control cash flow during downturns through reduced working capital and capital spending commitments, especially relative to debt. We have used this analysis while increasing our exposure to economically-sensitive stocks whose prices have declined significantly (industrials, consumer discretionary, and some energy). As a result, our exposure in these sectors has increased from 10.6% (third quarter, 2019), to 23.3% today.

To summarize, we are trying to navigate higher prices caused by increased liquidity from the Federal Reserve, and reduced cash-flow among more attractively priced stocks being impacted by COVID. Political risks are rising as well. Our focus is on owning companies with long-term growth records at fair prices that can remain cash-flow positive despite a severe downturn. Our cash has risen back to 12% (about where we started the year) because it is becoming increasingly difficult to find stocks that offer growth, value, and quality.

Model Portfolio Changes & Characteristics

Our model holdings have experienced more turnover than normal due to economic and market volatility. Rather than detailing specific portfolio changes, it is more important to see the bigger picture, as represented by overall portfolio characteristics.

Key Characteristics ³		
30-Jun-20		
	BI&R	R1000 Value
Market Cap (\$, Bil.)	105.5	114.1
Active Share	92%	-
Forward P/E	14.9x	20.5x
Dividend Yield	2.4%	2.6%
Dividend Growth (10 Yr.) ^A	14.4%	11.9%
Net Debt / EBITDA ^B	2.0x	3.1x
Return on Assets (5 Yr. Avg)	7.2%	5.6%
^A Last 10 years		
^B Net debt after cash and investments		

**More Growth
Less Leverage
High ROA**

Historically, our portfolios have sacrificed some yield to own firms with more growth, less debt versus income, and a higher return on assets. Higher return on assets and growth generally reflect a healthier and more attractive business franchise. A company with less debt versus income should have less operating risk.

Our low forward P/E today versus the index (14.9x versus 20.5x) reflects the greater stability of earnings for our holdings versus the typical Russell 1000 Value stock. The high forward P/E for the average Russell 1000 Value stock is due to reduced earnings estimates, not increased prices.

We believe these portfolio characteristics have provided the attractive risk-return profile of portfolios I have managed since 1986, namely, above-market returns combined with below-market volatility. BI&R portfolios offer continuity of the decision-making from my original firm, that is, from EIC (founded and registered in 1986). A copy of our June 30 All-Cap Value model portfolio is attached.

Conference Call

We will host a conference call on July 30 at 4:30 pm (EST). You may listen at (602) 609-9483, or participate online at <https://join.startmeeting.com/barksdale>. (Meeting ID = Barksdale) Please [reply](#) if you would like to receive a PDF of the slides before-hand or the replay link.

To learn more about BI&R's investment services, please visit www.BarksdaleInvestment.com.



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Equity Investment Corporation (12/31/85 to 9/30/16)

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Disclosures

¹ In the Horizon Asset Management LLC SEC No-Action letter (available September 13, 1996, (<https://www.sec.gov/divisions/investment/noaction/1996/horizonasset091396.pdf>), the Controlling Manager is the individual who holds final authority for investment decisions for a firm or strategy. When one firm wishes to advertise the performance achieved at another, but the investment committee changes, this guidance requires continuity of investment decision-making authority across firms to prevent violations of the SEC Rule 206(4)-I(a)(5) (The Advertising Rule). The Horizon letter explains that continuity of all investment committee members between firms is not necessary so long as a consensus of committee members was not required for investment decisions, and so long as there is continuity of the individual who held that final decision-making authority. Jim Barksdale was the Controlling Manager for all investment decisions made at Equity Investment Corporation (EIC – founded and registered in 1986). According to its SEC ADV filing: "Team members meet informally on a regular basis to discuss investment decisions. ... Jim Barksdale retains final investment authority over all investment decisions. Andrew Bruner, Terry Irrgang and Ian Zabor report to Jim." (Page 18 of Form ADV, Part 2, dated March 2, 2016). For additional information, See BI&R's "Frequently Asked Questions", available upon request.

BI&R only advertises results for strategies and periods in which Jim Barksdale was Controlling Manager.

Disclosures (cont'd)

² Jim Barksdale was Controlling Manager, holding and exercising sole veto and decision authority over all investment decisions for all investment strategies at Equity Investment Corporation (original-EIC, registered 1986) from January 1, 1985, through September 30, 2016. During this time, the firm's All-Cap Value strategy earned 11.9% per year versus 10.5% and 10.4%, respectively, for the benchmark Russell 3000 Value and S&P 500 indices, based on monthly gross returns reported to Morningstar. He was assisted by three additional investment team members who joined original-EIC (registered 1986) in 1999, 2003, and 2005.

Beginning October 1, 2016, original-EIC's accounts were assigned to a newly registered RIA (now also named EIC, registered 2016). Barksdale was not on the new firm's investment team for unrestricted strategies (All-Cap Value, Large-Cap Value, and Mid-Cap Value) nor involved in these investment decisions (formally or informally). However, Barksdale continued as Controlling Manager (sole decision authority) over investments for four socially responsible (restricted) strategies (Environmental, Human Rights, Catholic, and Protestant). BI&R advertises results from the least-restrictive of these strategies (Protestant Value). From October 1, 2016, until December 31, 2018, composites at EIC (registered 2016) for its Environmental, Human Rights, Catholic, and Protestant strategies increased 17.0%, 14.6%, 16.9%, and 17.6% respectively versus 11.3% for the Russell 1000 Value index. During this time, the Protestant Value portfolio that BI&R advertises increased by 17.3%.

From January 1, 2019, until June 30, 2020, the results are those of a separately managed account whose holdings and weightings follow BI&R's recommended U.S. Equity Value Model Portfolio. All figures are time-weighted returns, gross of management or administrative expenses. Cumulative results include reinvestment of dividends. Past results do not imply nor guarantee future results. Barksdale Investment & Research publishes model portfolios, does not tailor investments to client circumstances, and is not a Registered Investment Advisor. Subscriber results may vary depending on the individual implementation of published model portfolios. All investing involves risk, including the risk of loss.

³ Source for portfolio characteristics, sectors, and attribution is Standard & Poor's Capital IQ service.