CORNERSTONE
INVESTMENT PARTNERS, LLC

Why Active Value Now

Executive Summary

Value stocks remain extremely cheap relative to growth stocks, creating an attractive opportunity set for value-oriented active managers

Within value, we believe that active management has outperformed the Russell 1000 Value Index over the long term

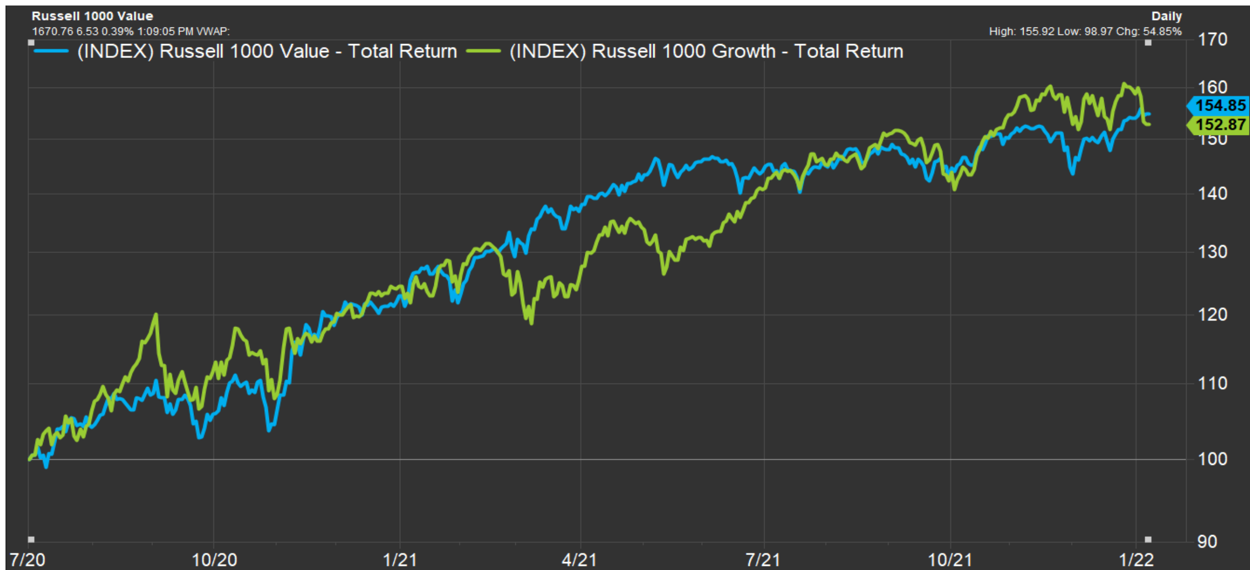
The S&P 500 is concentrated and expensive, placing owners of the index at risk of significantly underperforming value-oriented active management over the next several years

Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.

Value's Opportunity Set Remains Extremely Attractive.

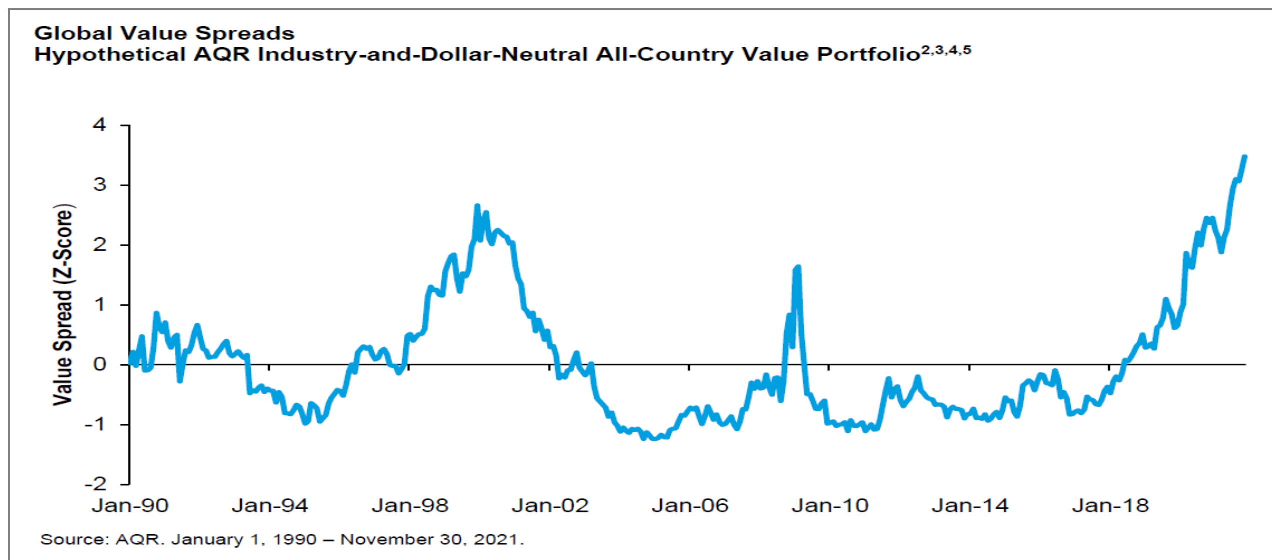
Over the past few years, we have written extensively about the outperformance of growth stocks over value stocks and the high valuations at which growth stocks trade. *Unsurprisingly, growth's outperformance over the last several years remains extreme, and growth's valuations remain excessive.*

Below, we detail the performance of growth vs. value since we released our last thought paper on the subject in July 2020. While imperfect, the Russell large cap style indices have delivered similar performance since the end of that month.



Source: FactSet

For valuation, we utilize AQR's exceptional work, which suggests that growth stocks remain as expensive as they've been in the last three decades relative to value stocks.



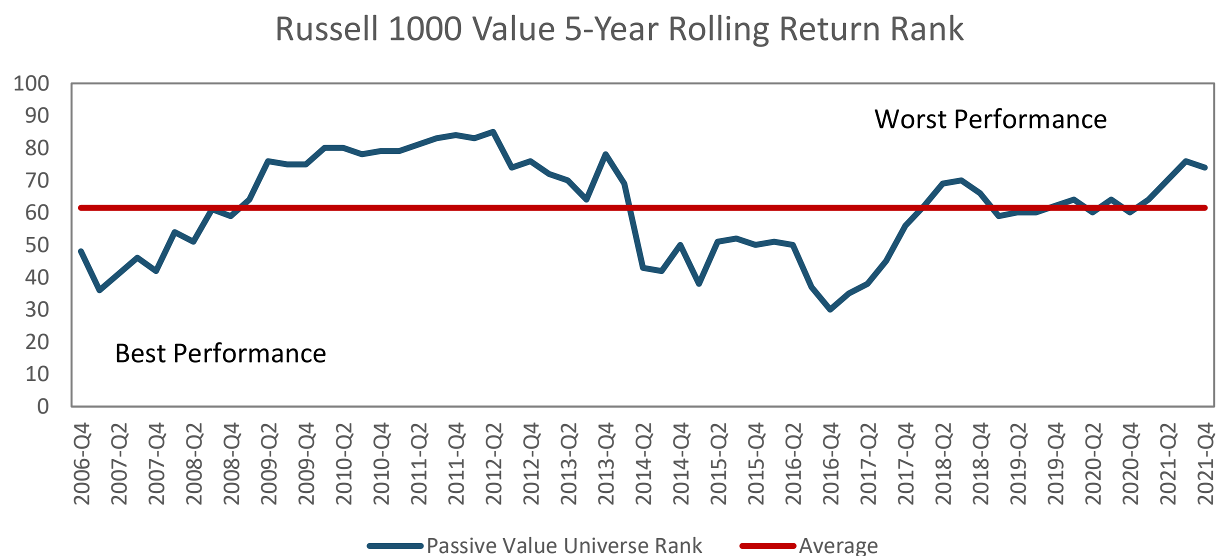
Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.

Over time, growth and value move in cycles. Growth outperforms for a period of time, and then cedes the lead to value. At times, the valuation spread between growth and value is wide and at times it is narrow. The pendulum swings too far in both directions, and presently the data suggest that it has swung too far in growth's favor. *As a result, the market has presented value investors with one of the most attractive opportunity sets our team has experienced.*

Now is the Time to Allocate to Value. Within Value, We Believe Active Management is the Superior Option.

Active management has meaningfully outperformed the Russell 1000 Value Index over the long term. Below, we present the Russell 1000 Value Index's rank within the eVestment Large Cap Value Universe on a rolling 5-year basis. The Russell 1000 Value Index has spent significant time in the bottom half of the universe and limited time in the top half of the universe, let alone the top quartile.

We believe a high-caliber active value manager is a better option than the Russell 1000 Value Index for allocators who wish to capitalize on the extremely attractive opportunity for value.



Source: eVestment

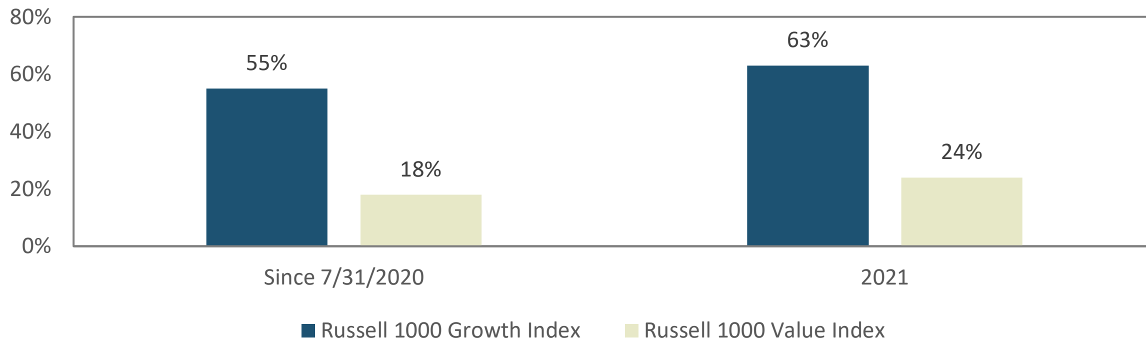
At Cornerstone, our investment process allocates capital to outstanding companies that trade at discounts to our conservative estimates of their intrinsic value. Our value orientation and our long-term investment horizon serve as our strategy's two greatest advantages, and we have designed our entire firm to ensure that we do not waver during periods of stress. Instead, we remain steadfast in our commitment to our value-oriented strategy.

<u>We believe that the current opportunity for our strategy is the kind that only arises a few times in a career and that we are well positioned to capitalize on this opportunity.</u>

Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.

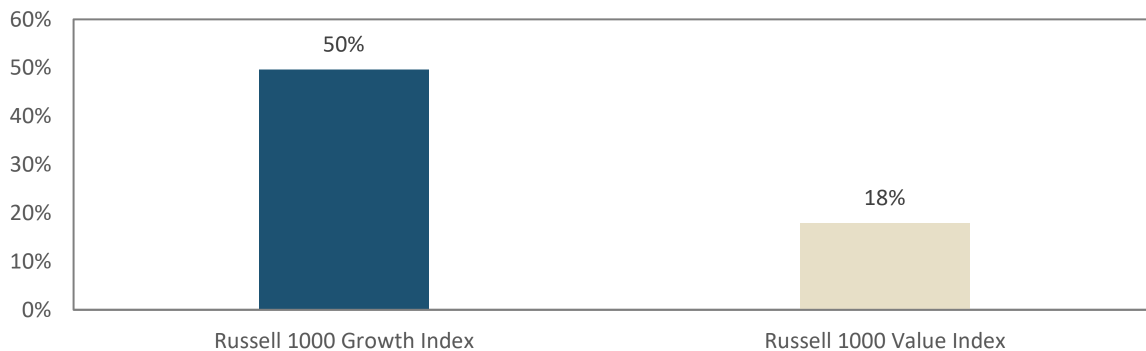
Growth is Concentrated and Expensive. The S&P 500 Shares This Risk.

While the growth and value indices have performed similarly since the end of July 2020, the composition of the leadership across the two indices has been markedly different. A small number of stocks have driven the performance of the growth index, while a much larger group of stocks have driven the performance of the value index.



Source: FactSet

Growth's narrow leadership has created a much more concentrated benchmark portfolio relative to value. The ten largest companies in the Russell 1000 Growth Index currently represent around half of the portfolio, while the ten largest companies in the Russell 1000 Value Index represent less than 20% of the portfolio.



Source: FactSet

There is nothing inherently wrong with portfolio concentration, so long as investors choose their large positions and properly monitor them. Passive indices do not choose their largest positions and they do not monitor them. If fundamentals deteriorate at one of the largest companies, the index will not exit the position. *As a result, investors in concentrated indices with lofty valuation characteristics face significant risk of permanent capital impairment.*

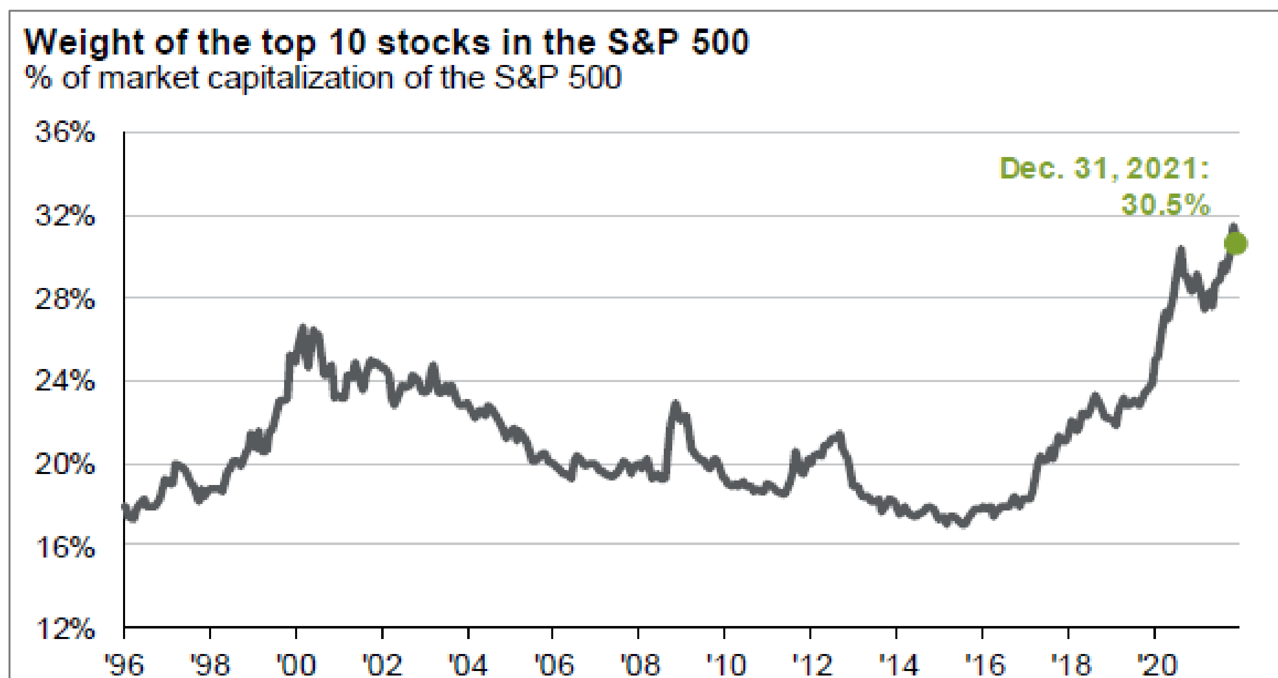
Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.

CORNERSTONE
INVESTMENT PARTNERS, LLC

The S&P 500 is also Concentrated and Expensive.

The S&P 500 is highly concentrated at present. The top 10 companies represent over 30% of the index. Seven of the top ten companies in the S&P 500, representing over 27% of the portfolio, are among the ten largest companies in the Russell 1000 Growth index.

To be clear, most of these companies are impressive operations. We own several today and have owned others in the past as our valuation process has allowed. That being said, we believe that paying too much for even a great company puts an investor at risk of permanent capital impairment. Commentary on individual stocks is beyond the scope of this paper, but our investment team will happily discuss them with you if you would like.

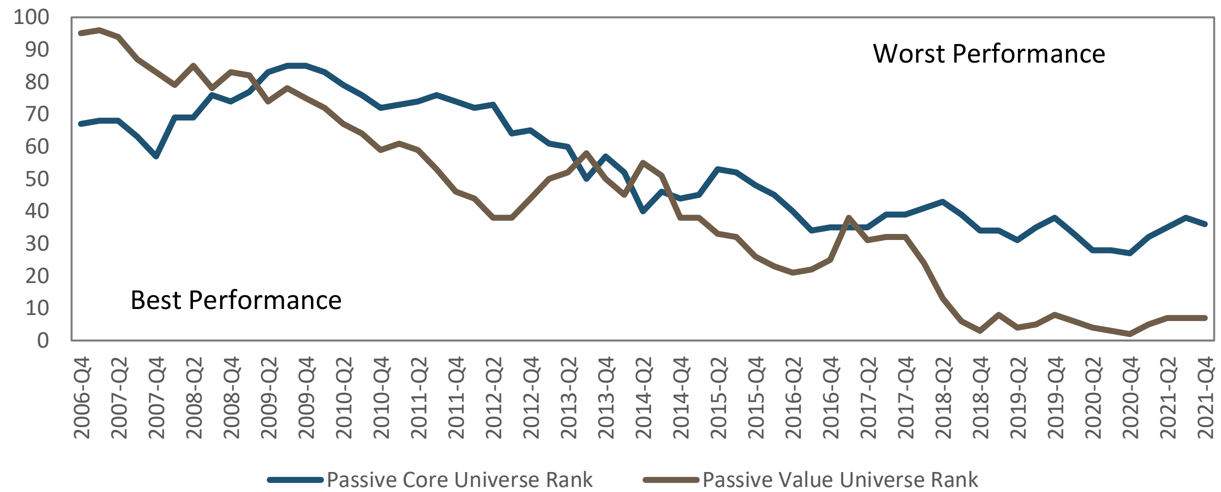


Source: J.P. Morgan

We've seen this setup before. During the internet bubble, the S&P 500 became highly concentrated, expensive, and sported a distinct growth tilt. *Subsequently, the S&P 500 underperformed the overwhelming majority of active managers and both the core and value universes for several years.*

Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.

S&P 500 5-Year Rolling Return Rank



Source: eVestment

Once again, we believe that the current opportunity set for value is highly attractive and, within value, active management has delivered superior performance, relative to passive. The leadership of a small group of richly priced stocks has led to a high degree of concentration within both the Russell 1000 Growth Index and, more importantly, the S&P 500. The present composition of the S&P 500 places the index at risk of significantly underperforming value-oriented active management over the next several years.

Past performance does not indicate future results. As with all investments, the possibility for profit is accompanied by the risk of loss.