



CAMPBELL NEWMAN

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# LARGE CAP DIVIDEND GROWTH 2Q 2021 COMMENTARY

## MARKET OVERVIEW

Stocks continued to march higher in 2Q 2021, driven by the ongoing “reopening” of the economy and plentiful liquidity. Positive returns were broad-based across market caps and by style with the S&P 500 providing an 8.55% return while achieving all-time highs. Growth outperformed Value in each of the Russell size indexes except Microcap, while Large caps generally outperformed Mid and Small caps.

As it became evident that the rate of change in economic and earnings growth from March 2020 was peaking, the market rotated away from some of the more cyclical stories in the Industrials and Materials sectors. Energy, however, followed through from last quarter as one of the top performers (11.30% return), as the price of oil (WTI) increased roughly 24% to over \$73/bbl by June 30. Other outperforming S&P 500 sectors included Real Estate (13.09%), Information Technology (11.56%) and Communication Services (10.72%). The Utilities sector recorded the only negative quarterly return of -0.41%.

Inflation ticked up in the quarter, with the CPI rising from 2.6% in March to 5.0% in May, a level not seen since 2008. It is unclear whether higher inflation is here to stay, as the result of all the monetary and fiscal stimulus, or if it is transitory, largely a result of a shorter-term lag from factories’ rebuilding capacity to catch up to demand growth. It is noteworthy that the yield on the bell-weather 10-Year Treasury declined by 16% in the quarter to 1.45% from 1.74%. However, while changes in interest rates would normally provide clues regarding inflation expectations, we have less confidence in their predictive ability due to the Fed’s ongoing market intervention.

## PORTFOLIO REVIEW

The Large Cap Dividend Growth portfolio took part in the market’s strong rally with a net of fees return of 7.60% modestly underperforming the S&P 500’s 8.55% return. This



relative performance is not unexpected in a “risk on” environment when the Russell 1000 Growth Index’s performance (11.93%) was more than double that of the Russell 1000 Value Index (5.21%). The Dividend Growth strategy is designed to outperform the S&P 500 over a market cycle at lower levels of volatility by participating on the upside while protecting to the downside. The portfolio only includes the stocks of companies with a history of consistent annual dividend increases, is managed to have a S&P 500 dividend yield or greater, and the strategy’s bottom-up stock selection process utilizes a rigorous valuation discipline.

That said, stock selection in the Information Technology sector explains the relative underperformance and was caused by a handful of holdings in the semiconductor space, such as KLA Corp. (KLAC, -1.59% return), Texas Instruments (TXN, 2.33%) and Broadcom (AVGO, 3.62%). As such, the portfolio’s sector return was 7.23% vs. 11.56% for the S&P sector, costing over 170 bps relative. The CN investment team sees this short-term performance lag as part of the market’s regular push-and-pull since each of the portfolio holdings continues to execute well while serving growing end-markets.

## TOP CONTRIBUTORS

**Microsoft Corp. (MSFT)** reported strong fiscal 3Q 2021 results across the board and ahead of expectations and guidance, with the all-important cloud computing service, Azure, growing by more than 50% Y/Y. Key forward-looking bookings and backlog metrics which drive future recurring revenue growth looked strong as well.

**American Express Co. (AXP)** reported 1Q 2021 EPS of \$2.74, exceeding consensus expectations of \$1.62. Management upwardly revised 2021 earnings guidance and exhibited strong conviction in attaining their 2022 earnings goal of \$8.85-\$9.25 per share.

**Apple, Inc. (AAPL)** reported fiscal 2Q 2021 results that exhibited broad-based strength across all segments. 5G adoption drove iPhone sales while the WFH environment continued to drive Mac and iPad sales. Services growth accelerated helped by a larger installed base and engagement across its wider offerings.

## BOTTOM CONTRIBUTORS

**KLA Corp. (KLAC)** reported fiscal 3Q 2021 financial results above consensus on better-than-expected process control equipment demand. Fiscal 4Q 2021 guidance was also above consensus on continued demand strength. Overall, the results and guidance reflect the diversified strength of the business and its strong product cycles.

**Abbott Laboratories (ABT)** issued updated 2021 guidance during the quarter reflecting decreased COVID-19 testing expectations. While disappointing, we see Abbott positioned to weather the volatile demand environment with its business split evenly between more traditional medical technology and its consumer-oriented franchises like diabetes.

**Regions Financial Corp. (RF)** did not change its full-year revenue forecast after reporting better-than-expected 1Q 2021 results as higher non-interest income was offset by lower net interest income. Bank stocks, in general, gave up some of their gains in the quarter as the yield curve began to flatten after the Fed raised the possibility of earlier than expected rate hikes in response to reports of higher-than-expected inflation. Nonetheless, RF is well situated to take advantage of its higher-growth Southeastern markets, strong consumer deposit base and balance sheet.

## PORTFOLIO POSITIONING

Portfolio positioning changed little in the quarter with turnover of 1%. Lockheed Martin (LMT) was trimmed to add to Comcast (CMCSA) and Organon (OGN), a spin-off from Merck & Co. (MRK), was sold because it did not meet the strategy’s investment criteria.

Built through bottom-up stock selection, the Dividend Growth portfolio sector weights reflect where the team has identified the most attractive risk/return opportunities within the strategy’s investment parameters. The portfolio continues to be focused on Information Technology (39.7% weighting), Financials (16.7%), Health Care (14.3%) and Industrials (12.0%). These sectors are also overweighted relative to the benchmark.



## TOP AND BOTTOM ABSOLUTE CONTRIBUTORS

2Q 2021 TOP CONTRIBUTORS	WEIGHT	RETURN	IMPACT
Microsoft Corp.	5.43%	15.15%	80 bps
American Express Co.	4.44	17.44	73
Apple, Inc.	5.57	12.32	68
American Tower Corp.	3.60	14.09	50
Eli Lilly & Co.	2.11	23.30	48

2Q 2021 BOTTOM CONTRIBUTORS	WEIGHT	RETURN	IMPACT
KLA Corp.	3.78%	-1.59%	-7 bps
Abbott Laboratories	1.91	-2.89	-6
Regions Financial Corp.	1.94	-1.57	-3
Mastercard, Inc.	1.66	2.66	4
Honeywell International, Inc.	4.13	1.46	6

### LARGE CAP DIVIDEND GROWTH COMPOSITE PERFORMANCE NOTES:

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