TRIBUTARY CAPITAL MANAGEMENT

# LARGE CAP EQUITY MARKET COMMENTARY

**PORTFOLIO MANAGERS: DONALD RADTKE & NICHOLAS NEVOLE**

**FIRST QUARTER 2024**

| | Quarter | Year to Date | 1 Year | 3 Years | 5 Years | 10 Years |
|---|---|---|---|---|---|---|
| Tributary Capital Management (Gross of Fees) | 7.1% | 7.1% | 22.3% | 10.3% | 13.8% | 11.3% |
| Tributary Capital Management (Net of Fees) | 6.9% | 6.9% | 21.6% | 9.6% | 13.0% | 10.6% |
| S&P 500 Index | 10.6% | 10.6% | 30.0% | 11.5% | 15.1% | 13.0% |
| Russell 1000 Index | 10.3% | 10.3% | 29.9% | 10.5% | 14.8% | 12.7% |

## MARKET REVIEW

The market is off to a strong start this year as investors point to increased optimism surrounding an economic soft-/no-landing scenario, a fourth quarter earnings season that exceeded expectations, and continued artificial intelligence (AI) momentum. Though first quarter guidance was a bit weak, many management teams are still expecting their end markets to recover in the back half of the year. The expectation of a recovery was enough to send some of the more cyclical areas of the market higher in the back half of the quarter.

Growth stocks outpaced value again this quarter, though both generated healthy returns (Russell 1000 Growth +11.4% vs. Russell 1000 Value +9.0%). Market performance broadened out as the quarter progressed, and the S&P 500 Equal Weight Index finished +7.9%. With that said, market concentration cannot be overlooked. AI-bellwether NVIDIA continues to climb the ranks in terms of market cap as its strong performance resulted in a nearly 5.0% weight in the S&P 500 Index to close the quarter, trailing only Microsoft and Apple for the index's largest constituents. The stock's +82% return in the first quarter had a notable impact on benchmark performance.

Communication services was the top performing sector for the S&P 500, +16% for the quarter. The performance was driven by continued momentum at Meta as well as strength out of several entertainment stocks. Energy was +14% for the quarter as the stocks benefited from rising oil prices. Meanwhile, information technology was up +13% driven primarily by NVIDIA and select other chip names.

The Tributary Large Cap Strategy generated a total return of +7.1% (gross return) for the quarter, unable to keep pace with the S&P 500's +10.6% total return. Over half of this relative underperformance was driven by not owning NVIDIA, the primary beneficiary of AI-related investment spending. From a relative perspective, the strategy's three weakest performing sectors included information technology (+3% vs. +13%), healthcare (+2% vs. +9%) and financials (+9% vs. +12%). While the bulk of the information technology underperformance was due to our lack of exposure to NVIDIA, our electronic equipment and instruments holdings also lagged. These names have underperformed as expectations for end market recoveries have been pushed further into the future.

Relative performance within the healthcare sector lagged due to a combination of our life sciences and healthcare equipment exposure. Sentiment surrounding potential growth in weight loss drug demand also caused our pharmaceuticals exposure to lag. Lastly, our financials sector underperformed primarily due to adverse reserve developments reported by Markel. While the stock recovered from its initial sell-off from the announcement, it was not enough to keep pace with peers which did not face similar headwinds.

The strategy did have positive relative performance within consumer discretionary, real estate and communication services sectors. Consumer discretionary (+11% vs. +5%) benefited primarily from not owning Tesla which was -23% in the quarter from company-specific issues and weaker electric vehicle sentiment. Real estate (+3% vs. -1%) outperformed as we do not currently own any REITs, which have lagged as investors shifted toward a higher-for-longer interest rate sentiment. Lastly, communication services (+15% vs. +16%) was the top performing sector on an absolute basis, and we benefited from our overweight positioning and Disney holding.

## PORTFOLIO CHANGES

During the quarter, there were no additions and one elimination made to the portfolio. *Global Payments*, a payment processing company, was sold to fund more attractive opportunities within the portfolio and to reduce the strategy's overweight in the financials sector.

## TOP CONTRIBUTORS

**Meta Platforms** (Facebook) saw its stock rise on a quarterly earnings report that showed advertising strength across all geographies. They also instituted a new dividend and increased share buybacks.

**Microsoft** beat revenue, margins and EPS expectations partly on strong Azure (cloud) performance and integration of artificial intelligence into its many product offerings.

**Walt Disney** had a significant beat on EPS and management raised full year guidance for EPS, driven in part by improved margins for its streaming operations. Also, management provided favorable guidance for subscriber additions for Disney Plus.

**Amazon** generated above consensus revenue, margins and EPS, driven largely by strong performance from its cloud computing division. Also, the company announced a number of artificial intelligence initiatives, improving sentiment for the stock.

**Eaton Corp.**, a leading diversified industrial manufacturer, continues to see strong demand with mega projects expected to drive significant market opportunities over the next few years. A strong backlog provides visibility as management invests for additional future growth.

## TOP DETRACTORS

**Apple** guided for weaker revenue in the next quarter due to foreign exchange headwinds and slower iPhone sales.

**Littelfuse**, a manufacturer of fuses and other circuit protection components, continues to see inventory destocking across its electronic and commercial vehicle distribution channels as well as at some of its OEM customers.

**Xcel Energy**, an electric utilities company, acknowledged its facilities were involved in the ignition of the Texas Smokehouse Creek Fire but disputes claims that it acted negligently, which is a key point in determining liability in Texas. Xcel's financial exposure has been estimated in the range of $2-5 billion. Wildfire risk is an issue that utilities are focused on addressing with industry-wide proposals and reforms.

**Robert Half**, a temporary staffing company, reported better than expected results in a slowing staffing backdrop. The downward industry trend continued into 2024, and the company issued first quarter guidance that is down from the prior year. Sequential improvement is expected through the rest of 2024.

**UnitedHealth Group**, a health insurer, physician group owner and physician services provider, missed quarterly operating profit expectations due to higher medical claim expenses that were driven by an increase in elective procedures and doctor visits. 2024 guidance was not changed, but investor anxiety increased regarding a lower-than-expected initial 2024 Medicare Advantage reimbursement rate proposal that will likely be revised upward. The Department of Justice also announced an anti-trust investigation into the company's business units and its vertically integrated business model. UNH also experienced a cyber security issue at its Change Healthcare unit in the quarter.

## PORTFOLIO OUTLOOK

The Federal Open Market Committee meeting in March gave investors more confidence that rate cuts are coming, despite inflation data in January and February that was hotter than expected. Only time will tell if inflation is stickier than anticipated or if the recent data are just bumps along the road. The Federal Reserve appears to be in a wait and see mode with a bias toward rate cuts, though not as many cuts as some pundits projected at the end of last year. Given the economy's continued strength and the Fed's expectation that inflation will continue to slow, it seems the Fed doesn't believe a recession is necessary to bring down inflation.

Investors were bolstered by this and the increase in the Fed's 2024 GDP growth projection, moving from 1.4% to 2.1%. On this news, markets moved higher following the Fed's press conference. The S&P 500's 10.6% return in the quarter was driven by better-than-expected earnings and strong margins. These results, improving corporate sentiment and solid economic data have supported the soft- or no-landing narratives and have replaced the mindset that only Fed rate cuts could fuel equity gains. A healthy economy could do the same.

Though widely expected, we anticipate that the first cut in interest rates will be embraced by investors. Lower rates may also beget increased M&A and IPO activity. Companies and investors have shown a pent-up appetite for these transactions as exhibited by the recent deals Capital One and Home Depot have made and the IPOs of Reddit and Astera Labs. These transactions may also hint at the strengthening confidence in the U.S. economy. If recession fears continue to fade, the labor force remains strong, inflation doesn't reaccelerate and the economy continues to march forward, markets should have good reason to continue moving higher.

The domestic economic outlook is attractive at this time and should be supportive of equities. However, just like the NCAA March Madness tournament, there is always the potential for spoilers. If inflation or economic growth continue to surpass the Fed's expectations, they may not deliver the rate cuts that are expected, which may cause investors to be more cautious. There has been unprecedented monetary tightening this cycle, which works with long lags. The November elections could also give investors a reason to pause as economic and regulatory policy may change dramatically depending on who is in control of Congress and the White House. Global tensions could also derail markets. Often, it seems the spoiler is one that few investors have in focus. Large cap equities have had a strong, uninterrupted upward move off last October's lows. So, it would not be surprising if the markets found cause for a breather sometime soon.

While we are well aware of the domestic and global issues that can move markets, we stay focused on what will drive the intrinsic value of our holdings over the coming years. At the end of the first quarter, the projected 2024 earnings growth for our strategy was 10%, a bit better than the 9% growth expected for large-cap stocks by Jefferies Research. Our stronger expected growth is paired with a 21.3x forward earnings multiple, only slightly above the 21.1x multiple for the benchmark. Our strategy is populated with high-quality companies possessing attractive valuations. These are the building blocks of investing that put our portfolio and our clients' capital in a strong position for the future.

*Unless otherwise noted, all returns, excluding Tributary Capital Management's strategies, have been obtained from FactSet Research Systems. Sector and security level performance is presented net of fees, using the highest potential fee an investor would pay.*

*The performance numbers shown above are for the Tributary Large Cap Equity Composite and are expressed in U.S. dollars. Due to the merger described below, the creation date of Tributary's Large Cap Equity Composite is Jan 1, 2005. The composite includes all discretionary accounts with an initial market value of $500,000 that are generally invested in a large capitalization equity strategy. The inception date of the Large Cap Equity Composite is March 31,1985. The Tributary Large Cap Equity Composite was formerly known as the Tributary Large Cap Value Equity Composite through periods ending March 31, 2019. The Standard & Poor's 500 is a basket of 500 stocks that are considered to be widely held. The S&P 500 index is weighted by market value, and its performance is thought to be representative of the stock market as a whole. The S&P 500® Equal Weight Index (EWI) is the equal-weight version of the widely-used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance. The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 companies with lower price-to-book ratios and lower expected growth values. The Russell 1000 Growth Index measures the performance of the large cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values. s today's modern day industrials. It is not possible to invest directly in the S&P 500, S&P 500EWI, Russell 1000 Index, Russell 1000 Value Index or the Russell 1000 Growth Index.*

*Net-of-fees composite returns are calculated using the highest potential fee the investment advisor will charge investors in the composite. Net performance is reported net of investment advisory fees and transaction costs. Capital gains and dividends are reinvested for performance calculations.*

*It should not be assumed that an investment in securities identified was or will be profitable or that the investment decisions we make in the future will be profitable or will equal the performance of the securities discussed herein. Holdings are subject to change. The holdings identified do not represent all of the securities purchased, sold or recommended for the portfolio. The holdings listed should not be considered recommendations to purchase or sell a particular security. The "Top Contributors" and "Top Detractors" represented are based on contribution to portfolio return. To obtain the contribution calculation methodology and a complete list of every holding's contribution to the overall portfolio's performance during the quarter, please contact clientservices@tributarycapital.com. Sector performance in commentary is stated gross of fees.*

*Tributary, an SEC Registered Investment Adviser, is the combined entity of the prior Tributary (formed Jan. 1, 2005) and First Investment Group (formerly a department of First National Bank of Omaha) which merged in May 2010. Tributary is a wholly owned subsidiary of First National Bank, a wholly owned subsidiary of First National of Nebraska, Inc. and manages mutual funds and equity and balanced portfolios. Tributary Capital Management, LLC ("Tributary") claims compliance with the Global Investment Performance Standards (GIPS®). A fully compliant report can be requested by emailing clientservices@tributarycapital.com.*

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