

Neuberger Berman Equity Income Team

PORTFOLIO MANAGERS: Richard Levine, Sandy Pomeroy, William Hunter, and Shawn Trudeau, CFA

Market Context

The historic correction triggered by the Coronavirus (COVID-19) has seen indices tumble from record high levels. Widespread uncertainty has impacted the global economy as nations, and policy makers alike take unprecedented actions.

When evaluating the return profile of the S&P 500, it's worth noting "growth" stocks with limited, and in many cases no dividend programs have broadly outpaced their "value" counterparts by a wide margin. Despite the challenging environment, we believe the selloff across the value complex has created a unique opportunity for investors willing to arbitrage time horizons. Today, we remain well positioned to capitalize on volatility as we have identified a number of companies now trading at compelling valuations with significant upside potential. We believe our flexible approach can drive performance through prudent stock selection during these challenging times.

In our view, there remains several "known, unknowns" related to the severity of the global contraction and its impact on supply chains, manufacturing, and consumption. Business across Asia, Europe and the Americas has come to a near standstill which will likely have a profound impact on cash flows, and investment activity. When evaluating investment candidates, our approach is focused on free cash flow and capital allocation plans. We believe this is the most effective means to understanding dividend programs, and ultimately their sustainability during both good and bad times. Amid the historic selloff, we have taken the opportunity to engage with management teams as we strive to high-grade our portfolio strategy by avoiding companies with excess leverage, and unsustainable payout ratios.

Investment Implications

The situation regarding COVID-19 remains fluid, and evolving by the hour. We remain encouraged by the dedication of scientists worldwide as they race to create a potential vaccine. Moreover, we believe actions by global central banks, and the probability for fiscal stimulus working in concert hold great potential to bolster sentiment.

Today, it is extremely difficult for our management teams to provide earnings visibility and guidance related to their business segments. However, we believe uncertainty varies across sectors and can create pockets of value. Through this lens, we have selectively rebalanced, while adding new investments, capitalizing on extreme price dislocations. In our view, risk-management is paramount as we strive to strike a balance between offensive and defensive elements. Recent liquidity challenges have seen dislocations across the Convertible Bond market, creating opportunities across what we believe are high-quality securities trading below par value. This hybrid asset class enjoys features similar to both stocks / bonds and within this sleeve we remain focused on names trading with reasonable yields, and attractive conversion premiums.

From a portfolio construction standpoint, high-quality businesses with stable cash flows including our defensive Utilities, Consumer Staples, and Health Care names seem to have dampened volatility. In several cases, we see our carefully selected electric-gas companies enjoy monopoly-like characteristics, providing high earnings visibility while giving investors exposure to infrastructure modernization as the United States embraces carbon-friendly fuels sources (Natural Gas / Renewable Energy). Relative to other sectors, the lion's share of revenues generated by most Utilities are US-Dollar denominated and this sector appears to be less-susceptible to global supply chain disruptions.

Elsewhere, we have trimmed several positions into strength including the second-largest producer of baked goods. On the Health Care front, the world is racing towards finding a potential vaccine for COVID-19. In response, shares of one of our notable drug-makers were bid-up as their antiviral drug received approval for clinical trials to treat COVID-19. Given this backdrop, our strategy eliminated its position, with the proceeds allocated elsewhere.

In closing, we thank you for trusting our investment strategy as we navigate today's cross-currents.

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