



Bear Market Preparedness: Know What You Own

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That was fast. After peaking at 3,386 on February 19, 2020, the S&P 500 Index declined by 26.7% in just sixteen trading days to officially start a bear market. This marks the sharpest descent into bear territory in history.¹ The selling of stocks in this period has often felt indiscriminate as market participants struggle to discount the economic impact of the COVID-19 pandemic in a near-vacuum of information. Reactionary investment decisions are not typically rewarded in such a market environment.

Rather, in times of market stress, it is crucial to ‘know what you own’ and focus on underlying, long-term business attributes. For Jensen, these factors include competitive advantages, balance sheet strength, and free cash flow consistency. Using this framework, we can compare stock price reactions with our existing knowledge of each individual business to identify market over- and under-reactions.

Company	Price Decline: 2/19/20–3/12/20
Emerson Electric	-34.7%
United Technologies	-32.0%
V.F. Corp	-33.6%
Johnson & Johnson	-15.8%
Becton Dickinson	-13.9%
General Mills	-6.1%
S&P 500 Index	-26.7%

Source: Jensen Investment Management

The above table displays absolute share price changes for the top-three and bottom-three decliners among the stocks held in the Jensen Quality Growth Strategy during the aforementioned period. As shown, all the portfolio stocks declined in the period, within a range of -6.1% to -35.7%.

Judging magnitude in such a short time period is challenging, but for both the largest and smallest decliners the market reaction appears to be directionally consistent with prospects for near-term business fundamentals. Emerson, United Technologies, and V.F. Corp serve cyclical end markets and are therefore financially sensitive to economic changes. On the other hand, Johnson & Johnson, Becton Dickinson, and General Mills cater to relatively inelastic customer demand. And, both Johnson & Johnson and Becton Dickinson stand to benefit from increased use of the global healthcare system.

¹ Source: <https://www.ft.com/content/d895a54c-64a4-11ea-a6cd-df28cc3c6a68>



However, there are examples in the portfolio where the market reaction appears disproportionately negative relative to the fundamental outlook. Two such examples are Accenture and Stryker Corporation, as shares of both companies declined more than the market during this period. Yet, we view both businesses as resilient and well-positioned relative to expected economic headwinds.

Company	Price Decline: 2/19/20–3/12/20
Accenture	-29.4%
Stryker	-31.5%

Source: Jensen Investment Management

Accenture is the world’s largest business and information technology consulting firm, serving clients in approximately 120 countries throughout the world including 75% of Global 500 companies. The company sports a nearly debt-free balance sheet, and its global scale allows for the unique combination of strategic advice and execution expertise when crafting and implementing business productivity projects. These projects tend to be long-term in nature and cannot be quickly shuttered based on near-term economic speed bumps. As a result, we expect to see some business slowdowns but not the financial disruption that appears to be reflected in its recent share price decline.

Stryker is a global leader in orthopedic implants, surgical tools, and hospital equipment, serving primarily hospitals and other healthcare delivery organizations. It benefits from longstanding product development and commercial relationships with these clients. Stryker also benefits from revenue diversity, both at the product and geographic level. We expect to there will be pockets of short-term challenges across its product portfolio, as some orthopedic procedures can be delayed. However, Stryker products support many non-discretionary procedures, and it is a global leader in the sale of hospital beds, a business that stands to benefit from higher hospital admissions.

Capricious market declines are unsettling to all of us. In such times, it is paramount to separate market ‘noise’ from business reality. We take comfort managing a portfolio of time-tested businesses backed by competitive advantages and financial resiliency. As investors, our job is to weigh long-term business strength relative to market expectations. During this short time period, we have been in the fortunate position to add to many of the fund holdings—including Accenture and Stryker—at what we consider deeply discounted prices.

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The contribution to performance of the Portfolio’s Top Contributors and Bottom Contributors was calculated by multiplying the security’s weight in the portfolio by the rate of return. If you wish to obtain a list showing the contribution of each holding in the representative portfolio or additional information about the calculation methodology, please contact Jensen Investment Management, Inc. at info@jenseninvestment.com

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