Benchmark Aware, Fundamentally Driven: U.S. Large-Cap Sustainable Value in a Changing Market



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U.S. Large-Cap Sustainable Value Strategy

August 2026

Fast Reading:

- The 2026 Russell reconstitution at the end of June significantly reshaped the Russell 1000® Value benchmark, adding major technology companies at meaningful weights. For the U.S. Large-Cap Sustainable Value Strategy, these shifts reflect changes in benchmark classification, not changes in the underlying fundamentals of the businesses.
- The Strategy's investment process is built on three core pillars: free cash flow generation, capital allocation discipline and valuation. These pillars guide how the team evaluates opportunities and manages risk in a more concentrated large-cap value market.
- Recent portfolio activity reflects investment conviction rather than index membership. The Strategy added Amazon, Charles Schwab and Tenet Healthcare where the team saw attractive fundamentals and valuations, while exiting Comcast and LKQ as the underlying investment theses weakened.

The June 2026 Russell reconstitution offered a revealing snapshot of how benchmark construction can reshape the large-cap equity landscape. Amazon became the largest constituent in the Russell 1000® Value Index at approximately 6%, while Apple and Microsoft entered at weights of 5.4% and 3.9%, respectively.[1] Together, the three companies came to represent roughly 15% of the benchmark—nearly equivalent to the combined weight of its ten largest constituents at the end of 2024.[2]

The changes reflected the benchmark's classification methodology rather than a sudden transformation in the companies themselves. They also materially altered the opportunity set for active managers, affecting sector exposures, portfolio positioning and relative risk even where no corresponding trades had been made. Changes of this scale matter, even when the investment process itself remains consistent.

Benchmark awareness is an important part of our investment approach. We assess how changes in the benchmark's composition and concentration affect the portfolio and how its risks are measured. At the same time, individual investment decisions remain grounded in our assessment of business fundamentals; sustainable free cash flow, disciplined capital allocation and valuation.

The reconstitution did not change how we invest; it clarified why our approach matters.

Where the Strategy stands today

The U.S. Large-Cap Sustainable Value Strategy remains focused on a relatively concentrated portfolio of large-cap companies that we believe can generate durable free cash flow, sustain a competitive advantage and allocate capital effectively. We seek to invest when the valuation offers an attractive prospective return and a margin of safety.

This discipline becomes particularly important when benchmark classifications change rapidly. A company can move from one style category to another without any corresponding change in its customers, competitive position, management team or ability to generate cash. The label may change; the economics of the business may not.

A company's inclusion in a value index does not necessarily make it attractive. Its exclusion does not necessarily make it unattractive. Our role is to determine whether the market price adequately reflects the durability of the company's free cash flow, the quality of its competitive advantages and management's ability to allocate capital.

The portfolio continues to evolve as evidence supporting individual investment theses changes. During the second quarter, we established positions in Amazon, Charles Schwab and Tenet Healthcare. We exited Comcast and LKQ Corporation when the original investment cases no longer offered the same degree of conviction.

This activity illustrates an important aspect of the process: consistency does not mean inactivity. It means applying the same investment criteria as facts, valuations and risks change.

What the benchmark reconstruction changed—and what it did not

The Russell reconstitution reshaped both the opportunity set and the way active risk is measured.

When a company receives a large benchmark weight, an active manager must assess the portfolio implications. A decision not to own the company, or to hold it at a lower weight than the index, may become a significant source of relative risk. That risk must be understood and managed.

That consideration matters from a portfolio construction and attribution perspective. It does not answer the central investment question: Does the company improve the risk-adjusted return of the portfolio?

Amazon illustrates how benchmark awareness and fundamental analysis work together. Amazon is a company we had been following closely for quite some time prior to establishing a position. We watched as the company's valuation continued to compress to multi year lows during the second quarter, despite what we believed were strong fundamentals. While we were

aware of the potential increase in the benchmark weight post the reconstitution, our decision to initiate the position was ultimately driven by our fundamental and valuation analysis.

Just like any other potential new investment, our analysis focused on the company's free cash flow generation potential long term. We identified improving free cash flow in the retail and international businesses, which we believed was obscured by concerns about near-term weakness in Amazon Web Services. We believed these concerns became more than priced in as the valuation had moved in line with the benchmark on an enterprise-value-to-EBITDA basis.

Together, those factors supported the investment case and while we were aware of the upcoming benchmark changes, fundamental analysis ultimately drove the decision.

The reconstitution also demonstrated how index methodology can influence capital flows. Index providers determine classifications, weights and implementation timing. Passive vehicles must then implement those decisions, regardless of valuation, concentration or changes in the underlying investment case. Index tracking may be passive in implementation, but the exposures investors receive are not static. A significant benchmark reconstitution can materially change what an investor owns without any corresponding investment decision on their part.

For active investors, that can create opportunities. Capturing them requires a consistent process grounded in the economics of individual businesses.

Our investment process

Our investment process is built on **three core pillars:**

1. **Free Cash Flow Generation.** We believe free cash flow is one of the clearest measures of a company's economic strength. It represents the cash remaining after the business has funded its operations and maintained the assets required to compete. The company can reinvest that cash, reduce debt or return capital to shareholders.

2. **Capital Allocation Discipline.** We evaluate how management deploys the cash a business generates. Capital allocation is one of the most consequential decisions within management's control.

   Strong businesses can destroy shareholder value through poorly conceived acquisitions, excessive leverage or undisciplined investment. Thoughtful reinvestment and responsible returns of excess capital can support value creation over time.

3. **Valuation.** We are not simply seeking companies that are statistically cheap. We look for situations in which the market may be underestimating the durability of a company's cash flows, the strength of its franchise or management's ability to improve returns.

These pillars are complemented by our Sustainable Cash Flow Advantage framework, which examines the "3Ps": **people** and culture, **processes**, and **products** and services. These considerations help us understand why a company's cash generation may persist. A strong culture can support execution and sound decision-making. Efficient processes can strengthen margins and resilience. Products and services that customers value can contribute to durable demand and pricing power.

The process in practice

Recent portfolio activity illustrates ways in which our process can identify opportunities.

Charles Schwab is a recent example of valuation discipline. Concerns about the potential effects of artificial intelligence contributed to share-price weakness and a significant valuation discount. Our analysis suggested that the company's underlying franchise remained intact, supported by its client asset base, cost culture and capacity to return capital. We believed sentiment had weakened more quickly than the fundamentals.

Tenet Healthcare presented a different opportunity. The company had improved its business mix, expanded margins and reduced leverage, while retaining exposure to long-term demand for healthcare services. In our view, its valuation and free cash flow yield did not fully reflect the progress in the underlying business.

Our sell decisions followed the same discipline. We exited Comcast after improvements in broadband performance proved slower than expected and competitive pressures intensified. We exited LKQ Corporation when the anticipated recovery and simplification initiatives did not develop at the pace that our thesis required. In each case, we redeployed capital because the fundamentals had changed, not because the benchmark had.

Why Fundamental Discipline Matters Now

As passive assets grow and benchmarks become more concentrated, index construction is likely to exert greater influence on capital allocation, market prices and the way active portfolios are evaluated.

Mechanical flows can move prices, but they cannot assess the durability of a company's cash generation, the quality of management's capital allocation or whether a valuation adequately compensates investors for risk. Those judgments remain the responsibility of the investor.

The Russell reconstitution changed the large-cap value landscape and the context in which active risk is measured. It did not change our investment philosophy.

We will continue to focus on businesses that we believe can generate sustainable free cash flow, allocate capital effectively and trade at valuations supported by disciplined research. The portfolio will evolve as the evidence changes. The process will remain consistent.

1. Source: FactSet® as of 06/30/2026.
2. Source: FactSet® as of 06/30/2026.

Disclosures

Portfolio level information is sourced from FactSet and based on a representative Large-Cap Sustainable Value account as of 06/30/2026. All investments involve risk, including possible loss of principal. Please see each product's web page for specific details regarding investment objective, risks, performance, and other important information. Review this information carefully before you make any investment decision.

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Terms and Definitions:

EBITDA (earnings before interest, taxes, depreciation, and amortization) is an alternate measure of profitability to net income. EBITDA attempts to represent the cash profit generated by a company's operations.

Enterprise Multiple (EV/EBITDA) is a financial ratio used to assess a company's value by comparing its total enterprise value to its earnings before interest, taxes, depreciation, and amortization (EBITDA).

Free Cash Flow (FCF) represents the cash a company generates after cash outflows to support operations and maintain its capital assets. Unlike earnings or net income, free cash flow is a measure of profitability that excludes the non-cash expenses of the income statement and includes spending on equipment and assets as well as changes in working capital.

Free Cash Flow Yield (FCF Yield) is a financial ratio that compares the free cash flow per share a company is expected to generate against its market value per share.

Margin of Safety is the difference between a security's market price and an investment team's estimate of its intrinsic value, typically expressed as the discount of the market price to that estimated value.

Valuation is the process of estimating the value of a company or security based on financial metrics, market factors and underlying assumptions.

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 and historical growth rates. The Russell 1000® Value Index is constructed to provide a comprehensive and unbiased barometer for the large-cap value segment. The Index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect value characteristics. The Russell 1000® Value Index and Russell® are trademarks/service marks of the London Stock Exchange Group companies. An investor cannot invest directly into an Index. Benchmark returns are not covered by the report of the independent verifiers.

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