Year End 2018 Commentary **Carol M. Lippman, CFA**

How Did We Do?

Our original research in the early 1990s—which formed the impetus for this strategy—showed that in challenging markets, rising dividends helped cushion returns. We are pleased to report that in a volatile period, the power of rising dividends helped cushion our returns.

Here are the performance results of our two Dearborn Partners separately managed account portfolios (SMAs) and the S&P 500 Composite Index ("S&P 500," the benchmark against which we compare our portfolios) for the fourth quarter followed by longer periods as of December 31, 2018.

Fourth Quarter 2018 Total Returns (%) as of December 31, 2018[1]

	Gross	Net
Core Rising Dividend SMA	*-10.2*	*-10.5*
High and Rising Dividend SMA	*-6.7*	*-7.0*
S&P 500[2]	*-13.5*	

Total Returns Annualized (%) as of December 31, 2018

	1- year		3- year		5- year		Since Inception (9/30/11)	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Core Rising Dividend SMA	*0.3*	*-1.3*	*9.4*	*7.7*	*8.5*	*6.8*	*12.2*	*10.4*
High & Rising Dividend SMA	*0.7*	*-0.9*	*10.4*	*8.8*	*9.3*	*7.7*	*12.4*	*10.7*
S&P 500	*-4.4*		*9.3*		*8.5*		*14.0*	

Staying the Course Is Critical When Investing in High Quality Portfolios

A December 11, 2018 Bloomberg News article titled, *Violent Stock Reversals Are Coming Faster Than Any Time Since 2011*[3] wrote:

> "Equity investors are getting used to whiplash.
>
> They got a dose today, when the S&P 500 wiped out a 1.4 percent rally. And the day before, when a 1.9 percent loss was erased. So far, there have been six days this quarter when stocks completely reversed an intraday move of at least 1 percent, the most since 2011, when Standard & Poor's downgraded the U.S. sovereign rating, sending stocks to the brink of a bear market."

[1] Returns are presented on a pure gross and net basis and include the reinvestment of all income. Pure gross returns do not reflect the deduction of any expenses, including trading costs, and are supplemental to net returns. Net of fee performance was calculated using actual fees, which include wrap fees, management fees and trading commissions. The Dearborn management fee schedule is 1.00% on the first $1 million and 0.75% on amounts over $1 million, but actual fees will vary.

[2] The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered to be representative of the U.S. stock market. Inclusion of this index is for illustrative purposes only. Historical performance results for investment indexes generally do not reflect the deduction of transaction and/or custodial charges or the deduction of an investment management fee, the incurrence of which would have the effect of decreasing historical performance results. Economic factors, market conditions, and investment strategies will affect the performance of any portfolio and there are no assurances that it will match or outperform any particular benchmark.

[3] https://www.bloomberg.com/news/articles/2018-12-11/violent-stock-reversals-coming-faster-than-any-time-since-2011

From Investopedia:

> "The term "bear market" is the opposite of a "bull market," or a market in which prices for securities are rising or will expect to rise. It is named for the way in which a bear attacks its prey — swiping its paws downward. This is why markets with falling stock prices are called bear markets. Just like the bear market, the bull market is named after the way in which the bull attacks by thrusting its horns up into the air.
>
> While there is no agreed upon definition of what makes a bear market, it's generally accepted that a bear market is characterized by a drop of 20 percent or more over a two-month period."[4]

Losing Less in Bad Markets Can Help

On September 20, 2018, the S&P 500 benchmark closed at a 52-week high of 2930.75. Its 52-week low of 2351.10 was reached on December 24, 2018, a 19.8% decline, or 20% in the rounding. Fifty-two percent of all companies in the S&P 500 declined 20% or more from their 52-week highs during this period. On the other hand, 39% of the companies in our Dearborn Partners Core Rising Dividend portfolio declined 20% or more from their 52-week highs; and 36% of the companies in our Dearborn Partners High & Rising Dividend portfolio declined 20% or more from their 52-week highs. Losing less money in challenging markets can help lead to portfolio outperformance.

In past Commentaries we have reviewed that our generally conservative, defensive strategy tends to hold up better than the benchmark on what we call "big down days" when the S&P 500 declined 1% or more. In all of year 2018, the broad market declined as much as 1% 32 times, or on 12.5% of the 257 trading days. Since inception through year-end 2018, the S&P 500 declined 1% or more on 162 days, or 8.8% of the 1,837 trading days during this period. Here is an update.

Big down days from inception (September 30, 2011) through December 31, 2018:

Total Days	1,837	
Total "Big Down Days" (down more than 1%)	162	
Total days that the Core Rising Dividend SMA ("CRD") outperformed the S&P 500 on "Big Down Days"	147	90.7%
Total days that the High & Rising Dividend SMA ("HRD") outperformed the S&P 500 on "Big Down Days"	143	88.3%

[4] https://www.investopedia.com/terms/b/bearmarket.asp

Cumulative Income Summary

Here is the cumulative gross (before fees) dividend income from an initial $200,000 investment on September 30, 2011 (the inception date of our SMA portfolios) through December 31, 2018 in each of:

	Average Current Yield	Cumulative Income*
Core Rising Dividend SMA	2.5%	$59,974
High & Rising Dividend SMA	3.3%	$77,843
S&P 500	2.0%	$53,865

***The S&P 500 dividend income in the table above is calculated by creating hypothetical investable "share units" by dividing the assumed initial $200,000 investment by the price of the index (1131.42) on September 30, 2011 (the inception date of our Rising Dividend SMA portfolios), resulting in 176.77 share units. The dividends per share unit of the index, provided by S&P Dow Jones Indices, are applied to the calculated units on a quarterly basis. The total represented in the table is the sum of those quarterly dividends per share unit, from December 31, 2011, through December 31, 2018.**

Dividend Increases

Core Rising Dividend SMA portfolio:

In the fourth quarter of 2018, 17 of the 49 companies in our Core Rising Dividend SMA portfolio announced 17 dividend increases averaging about 13.4% more than those particular companies paid a year before their latest dividend increase announcement date.

In all of year 2018, 48 of the 49 companies in our Core Rising Dividend SMA portfolio announced 62 dividend increases averaging about 13.3% more than those companies paid a year earlier. Throughout the year, three companies in this portfolio announced two dividend increases, two companies announced four dividend increases, and one company announced five dividend increases.

One company, CVS Health (CVS) did not raise its dividend in 2018 and has paid $0.50 per share for nine consecutive quarters. Through 2017, CVS raised its dividend at average compounded annual growth rates of 22%, 25% and 24% over the previous 3, 5, and 10 years, respectively. Then, on December 3, 2017 CVS announced its intention to acquire Aetna, Inc. (AET) for $68 billion in cash and stock. CVS took on so much debt that in order to maintain an investment grade debt rating, it likely cannot raise its dividend for many years until it significantly reduces its debt levels. We did not want to remove the CVS shares from our portfolio, however, until we were reasonably confident that regulators would allow the acquisition to go through. On October 10, 2018, CVS entered into an agreement with the U.S. Department of Justice that allowed it to proceed with its proposed acquisition of Aetna. On October 11, 2018, we replaced CVS with Casey's General Stores (CASY), which in June had already announced its dividend increase for 2018.

High & Rising Dividend SMA portfolio:

In the fourth quarter of 2018 in our High & Rising Dividend SMA portfolio, 9 of the 25 companies in the portfolio announced 9 dividend increases averaging about 13% more than those companies paid a year before their latest dividend increase announcement date. In all of year 2018, one company in this portfolio announced two dividend increases, one company announced four dividend increases, and one company announced five dividend increases.

In all of year 2018, 25 of the 25 companies in our High & Rising Dividend SMA portfolio announced 34 dividend increases averaging about 9.5% more than those companies paid a year earlier. Throughout the year, one company in this portfolio announced two dividend increases, one company announced four dividend increases, and one company announced five dividend increases.

A Premise for our Strategy

An objective of our strategy is to reduce vulnerability. Among the ways that we attempt to achieve that objective are to include in our portfolios companies that are in strong financial condition with little or no debt, that we believe are capable of increasing dividends at rates above the historic average annual 3% rate of inflation regardless of the economic environment, and to diversify properly across and within the sectors. We further believe that rising dividends offer the potential to reduce vulnerability in challenging markets.

At long last, the stock market has shown some cracks. A few largely non-dividend-paying stocks that have led the market for an incredibly long time have finally proven not to be invincible after all. Although past performance cannot assure future results, we believe that the solid companies in our portfolios are likely to not only survive long term but continue to pay dividends with the potential to increase with regularity. Successful investing typically requires patience. Every company in our portfolios pays us while we patiently hold.

Thank you for your interest in our Dearborn Partners Rising Dividend Strategy.

Research assistance provided by Jackson Finks, CFA and Matthew Guttosch, CFA

Dearborn Partners Rising Dividend Separately Managed Account
Average Calendar Year Dividend Increases

	Core Rising	High & Rising	CPI*
2012	13.0%	9.6%	1.9%
2013	12.2%	8.7%	1.7%
2014	12.2%	7.4%	1.6%
2015	9.7%	7.5%	2.1%
2016	8.0%	6.5%	2.1%
2017	7.8%	5.8%	1.7%
2018	13.3%	9.5%	2.2%

** Core Consumer Price Index for All Urban Consumers Unadjusted 12-month Percent Change. Year to Date (YTD) 2018 CPI through November.*

Source: U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers: All Items Less Food and Energy [CPILFENS], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CPILFENS December 12, 2018.

Disclaimer:

On the date that a company in our SMA portfolios announces a dividend increase, we calculate the percentage difference from the dividend the company paid a year earlier. We are excluding any special or accelerated dividends paid. We then calculate the average of all those year-over-year increases. However, if a company announces a dividend increase more than once a year, we use the average of that company's multiple increases to be considered in the year-over-year comparison.

Past performance is no guarantee of future results. Dividends are not guaranteed and must be authorized by the company's board of directors. Dividend yield is one component of performance and should not be the only consideration for investment.

This commentary presents general views on the securities markets and should not be construed as financial or investment advice on any subject matter. It is not a complete description of, not a recommendation to invest in, any investment strategy mentioned within. This commentary may not be redistributed without Dearborn's written consent. Some of the information herein has been obtained from third party sources. We believe such information is reliable, but we have not in each case verified its accuracy or completeness. All securities investing involves risks, and this commentary is not intended to address such risks. Dearborn may make securities recommendations to clients that are inconsistent with the views herein. Any opinions herein are as of the date of this report and are subject to change without notice. Dearborn Partners L.L.C. is an investment adviser registered under the Investment Advisers Act of 1940, as amended. Registration does not imply a certain level of skill or training.