DEARBORN PARTNERS

<u>Third Quarter 2019 Commentary</u> **Carol M. Lippman, CFA**

The Premise for Our Strategy

An objective of our Dearborn Partners Rising Dividend 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.

Sometimes we are asked why we hold so many stocks in our portfolios: 49 stocks in our Core Rising Dividend separately managed account (SMA) portfolio and 25 stocks in our High & Rising Dividend SMA portfolio. Our Rising Dividend portfolios have representation from all 11 sectors into which Standard & Poor's divides the marketplace. Proper diversification with stocks of high-quality companies can help modify downside risk, i.e., reduce vulnerability, and enhance results in both challenging and favorable market environments.

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.

How Did We Do?

It has been a good year for our Dearborn Partners Rising Dividend strategy, in our opinion. The total returns (price movement plus dividends, gross before fees) of both of our Dearborn Partners Rising Dividend SMA portfolios outperformed the benchmark S&P 500 in the third quarter and first three quarters (year-to-date) of 2019, as well as the one-year period ended September 30, 2019.

Third Quarter 2019 Total Returns (%) as of September 30, 2019[1]

	Gross	Net
Core Rising Dividend SMA	3.8	3.4
High and Rising Dividend SMA	4.5	4.1
S&P 500[2]	1.7	

Total Returns Annualized (%) as of September 30, 2019

	Year-to-Date		1- year		3- year		5- year		Since Inception (9/30/11)	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Core Rising Dividend SMA	23.6	22.2	11.1	9.4	13.0	11.2	12.0	10.3	14.0	12.2
High & Rising Dividend SMA	24.7	23.3	16.4	14.6	13.3	11.5	12.1	10.4	14.3	12.6
S&P 500	20.6		4.3		13.4		10.8		15.3	

Please keep in mind that over the past nine decades, the average **annual** total return for the S&P 500 has been about 11.8% according to Ned Davis Research. In **nine months** to have generated more than 20% is quite extraordinary. Our

[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.

portfolios generated what we consider to be respectable returns and outperformed the benchmark. Also please note that our portfolios' one-year returns outpaced the benchmark by a wide margin.

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 September 30, 2019 in each of:

	Average Current Yield	Cumulative Income*
Core Rising Dividend SMA	2.3%	$68,310
High & Rising Dividend SMA	3.1%	$89,078
S&P 500	1.9%	$61,471

**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 September 30, 2019.*

Interest Rates Remain at Historic Lows

Before the Federal Reserve implemented the zero-interest rate environment after the collapse of Lehman Brothers and the onset of the financial crisis in mid-September 2008, yields of relatively riskless investments were considerably higher than they are today. According to the Federal Reserve Bank of St. Louis, the secondary market rate on 6-month U.S. Treasury bills averaged about 5.6% from January 1962 through September 2008.[3] Ten-year U.S. Treasury bonds yielded an average 7% from January 1962 through September 2008 according to Macrotrends Data.[4]

In other words, people—who either could not afford or did not want to risk the volatility of the stock market—were able to get reasonably decent returns on their savings with relatively little risk if they held the securities to maturity. For the past decade, however, rates have been significantly lower. Since October 1, 2008, 6-month Treasury bill yields have averaged 0.6% and 10-year Treasury bonds have averaged 2.5%.

The Federal Reserve has been raising its Fed Funds rate (the short end of the yield curve) such that 6-month Treasury bills now yield around 2%. Yields at the longer end of the interest rate curve, however, have been under downward pressure as global growth and unrest, tariffs and other concerns have prompted a flight to safety. At the end of the third quarter on September 30, 2019, the yield on the 10-year U.S. Treasury bond stood at 1.67%. Core inflation, as measured by the latest Consumer Price Index for All Urban Consumers less food and energy (the measurement considered by the Federal Reserve) through August 2019 was up 2.4% year of year. In other words, those who invest in U.S. Treasury bills and bonds are not even keeping up with inflation. (As we are writing this Commentary in early October, the yield on the 10-year U.S. Treasury bond has dropped even more—to 1.53%, further exacerbating the ability to earn a real, inflation-adjusted return.)

As seen in the Cumulative Income Summary table above, the average current yields of our Core and High & Rising Dividend SMA portfolios of 2.3% and 3.1%, respectively, exceed the average 1.9% yield of the broad market and the 10-year U.S. Treasury bond. Although stocks are riskier and frequently more volatile than Treasury bills or long-term U.S. Treasury

[3] https://fred.stlouisfed.org/series/TB6MS
[4] https://www.macrotrends.net/2016/10-year-treasury-bond-rate-yield-chart

bonds, our SMA portfolios—with average betas of about 0.8—have historically been less volatile than the broad market as measured by the S&P 500. (The S&P 500 has an average beta of 1.0. An average beta less than 1.0 represents generally less volatility than the broad market. An average beta greater than 1.0 represents greater volatility.)

As a result of their lower volatility, above average yield and generally conservative features, our portfolios may appeal to some generally risk-averse investors who are in search of returns greater than those offered by long-term bonds with the full faith and credit backing of the U.S. Treasury. We thought we would look at how many stocks in these portfolios ended the third quarter with yields above the 1.67% yield on the 10-year U.S. Treasury bond and the 2% Treasury bill (T-bill) yield. At the market close on September 30, 2019, 24 of the 25, or 96% of the stocks in our High & Rising Dividend SMA portfolio had current yields above the 1.67% yield on the 10-year U.S. Treasury bond; 18 or 72% had yields above T-bills. Thirty-five, or 71% of the 49 stocks in our Core Rising Dividend SMA portfolio had a current yield above the 1.67% yield at which the 10-year U.S. Treasury bond ended the quarter; 27, or 55% had yields in excess of T-bills. Our portfolios pay investors income. Furthermore, all the dividend increases paid by the companies in our portfolios help investors not only keep up with inflation but help them outpace the rising costs of living.

Dividend Increases

Core Rising Dividend SMA portfolio:

In the third quarter of 2019, 14 of the 49 companies in our Core Rising Dividend SMA portfolio announced 14 dividend increases averaging about 8.9% more than those particular companies paid a year before their latest dividend increase announcement date. In the first three quarters of 2019, 35 of the 49 companies in our Core Rising Dividend SMA portfolio announced 44 dividend increases averaging about 8.9% more than those particular companies paid a year earlier. Most companies that announce dividend increases do so after four quarters, but one company in our Core Rising Dividend portfolio announced a dividend increase after only two quarters; four companies have announced dividend increases after only one quarter, and one of those companies also paid a special dividend earlier this year.

High & Rising Dividend SMA portfolio:

In our High & Rising Dividend SMA portfolio, 6 of the 25 companies in the portfolio announced 6 dividend increases averaging about 5.8% more than those particular companies paid a year before their latest dividend increase announcement date. In the first three quarters of 2019, 15 of the 25 companies in our High & Rising Dividend SMA portfolio announced 20 dividend increases averaging about 6.2% more than those particular companies paid a year earlier. One company has announced four dividend increases so far this year, and another company has announced three dividend increases this year.

No companies in our portfolios have decreased their dividends so far this year.

Thank you for your continued interest in our Dearborn Partners Rising Dividend Strategy. We are grateful for your partnership.

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

Dearborn Partners Rising Dividend Separately Managed Account
Average Calendar 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%
YTD 2019	8.9%	6.2%	2.4%

** Core Consumer Price Index for All Urban Consumers Unadjusted 12-month Percent Change. Year to Date (YTD) 2019 CPI through August.*

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 Sept. 12, 2019.

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.

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