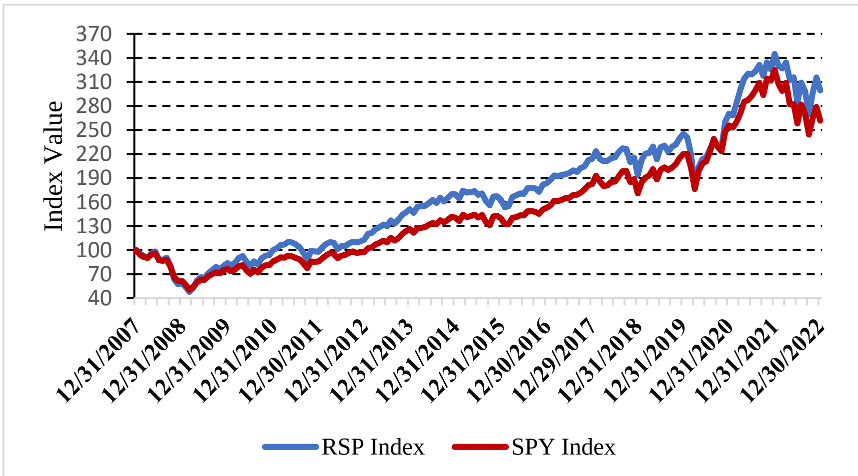
DEARBORN PARTNERS

Second Quarter 2023 Commentary **Carol M. Lippman, CFA**

Concentration of performance

For the 15 years from December 31, 2007 through December 31, 2022, as seen in Figure #1, the direction has been the same for the equal-weighted (ticker RSP, blue line) and the market cap-weighted S&P 500 (SPY, red line) indexes, with the equal-weighted index generally outperforming. In percentage terms, the average compounded total return over this 15-year period for RSP, +283.0%, outpaced SPY's +251.4%.

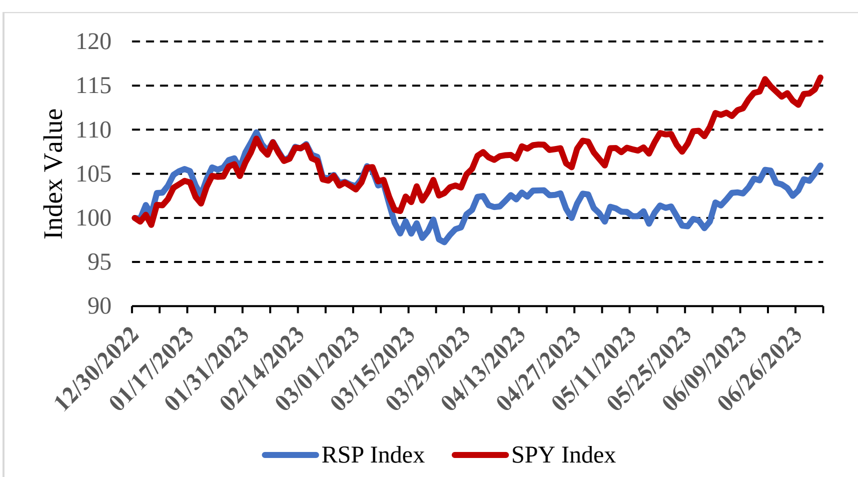
Figure #1: 15-Years Ended 2022 Prices of S&P 500 Equal-Weighted (RSP blue line) & Market Cap-Weighted (SPY red line) Indexes Dec. 31, 2007-Dec. 31, 2022



Source: FactSet

Figure #2 shows the first half of this year for these two indexes. Since mid-March, the market cap-weighted index (red line) significantly outperformed the equal-weighted index (blue line). In percentage terms, the compounded total returns of the two indexes were RSP +6.9%, SPY +16.9%.

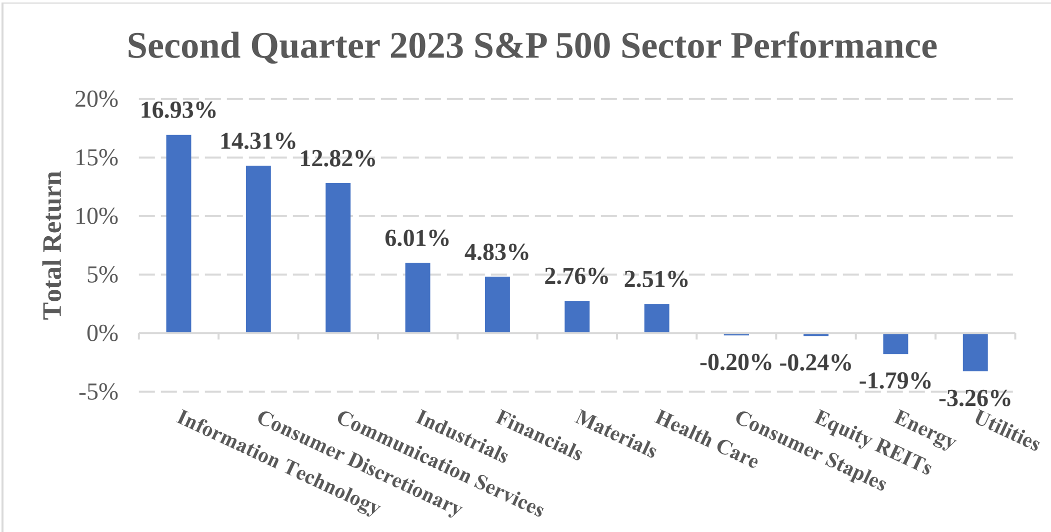
Figure #2: First Half 2023 Performance of S&P 500 Equal-Weighted (RSP blue line) and Market Cap-Weighted (SPY red line) Indexes Dec. 31, 2022-June 30, 2023



Source: FactSet

The breadth of market participation was poor in the second quarter of 2023. Figure #3 shows the dominance of a few sectors, led by technology, especially stocks of companies involved in creating semiconductor chips and software for a relatively new and evolving technology known as generative AI (artificial intelligence). The four sectors with negative returns in the quarter—Consumer Staples, Equity Real Estate Investment Trusts (REITs), Energy, and Utilities—generally consist of businesses that are considered more defensive, i.e., providing products and/or services that people patronize in tough times as well as good times. These four underperforming sectors include many companies that pay dividends.

Figure #3: S&P 500 Second Quarter 2023 Returns by Sector



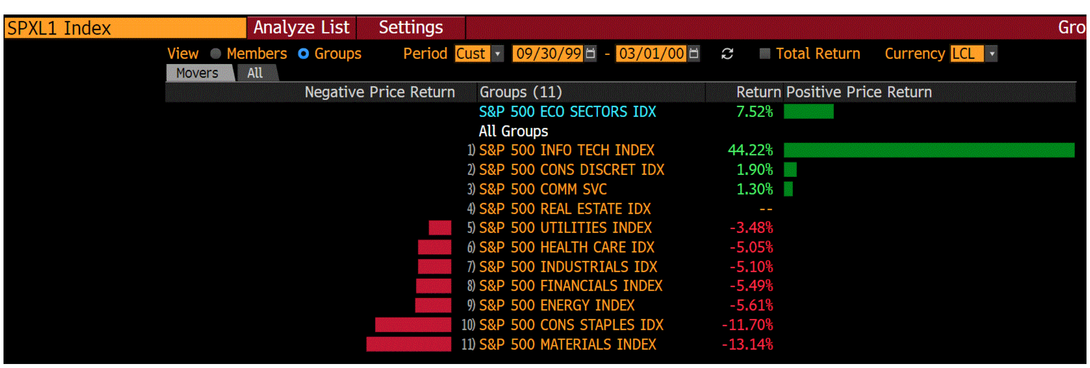
Source: FactSet

In Figure #4, Michael Kantrowitz of Piper Sandler shows the similarity of this year's sector performance with that during the peak of the dot.com stock market bubble from October 1999 through February 2000. We remember the dot.com era when dividends were considered passé. Déjà vu?

Figure #4: Déjà vu?

Sector Performance: 2023 Year To Date

Sector Performance: Sept. 30, 1999 – March 1, 2000



Source: Bloomberg, Piper Sandler Portfolio Strategy - Michael Kantrowitz

In fact, market breadth was very narrow in the entire first half of this year. Five mega-cap stocks—only two of which meet the stringent criteria for inclusion in Dearborn Partners' Rising Dividend Strategy—have been credited with much of this outperformance. Data from FactSet shows that in the first half of 2023 the total return of the S&P 500 Index was 16.86%. The median stock total return, however, was only 4.78%, and only 27.5% of stocks had total returns greater than that of the Index. Combined, Apple, Microsoft, NVIDIA, Amazon.com, and Meta Platforms contributed 60% of the benchmark's total return.

Strategas Research shows in Figure #5 that the combined weights of these five mega-cap stocks dominated the broad market as never before in the past three decades.

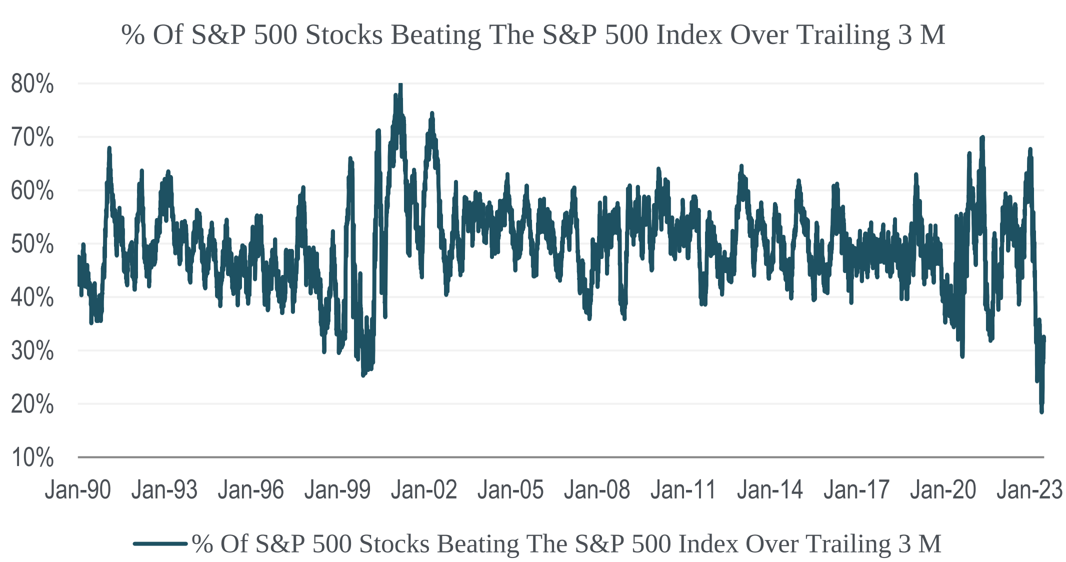
Figure #5: Unprecedented Benchmark Dominance by Only Five Large Stocks

Source: Strategas Research June 30, 2023 Quarterly Review in Charts

Figure #6 from Piper Sandler shows the narrowness of this stock market by illustrating that the fewest stocks have beaten the broad market index this year since the peak of the dot.com bubble in early year 2000.

In the history of the stock market, there have been occasional periods, usually relatively brief, in which just a few stocks dominated returns. As can be seen in Figure #6, most of the time over the past 30 years, for example, when roughly 40%-50% of stocks beat the S&P 500 Index, it has made sense to be invested in well diversified portfolios.

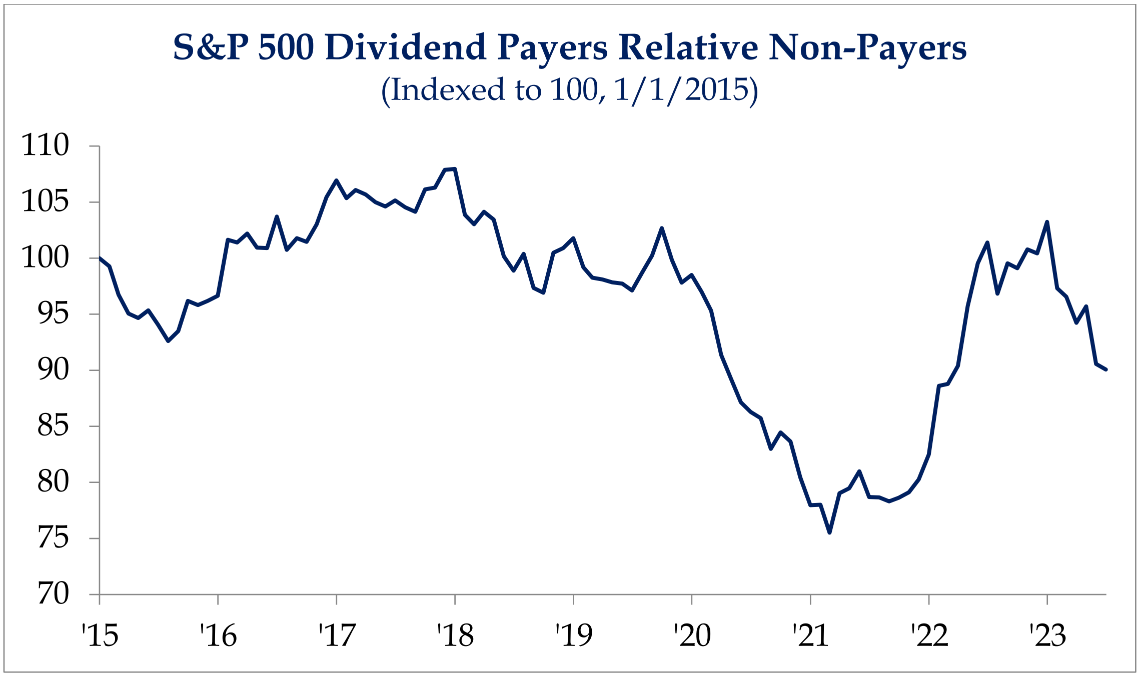
Figure #6: Fewest Stocks Beating S&P 500 Since March 2000

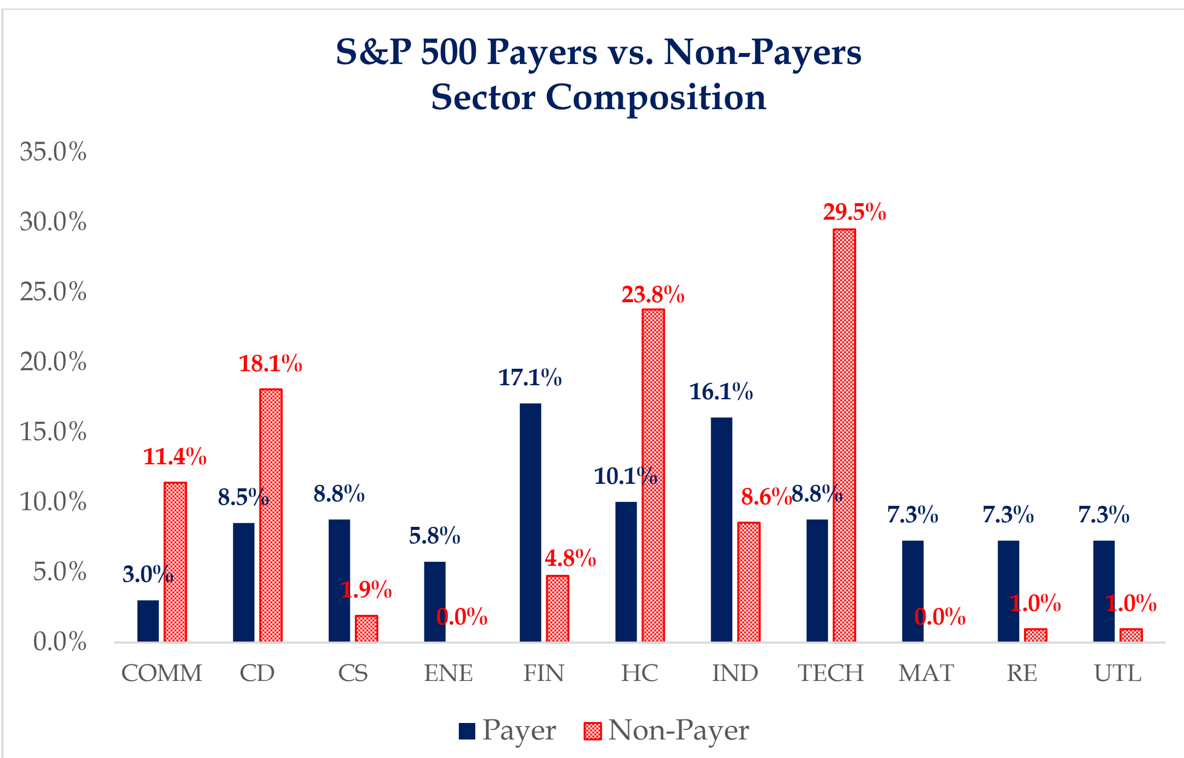


Source: Piper Sandler Cornerstone Macro Research

In Figure #7 Strategas Research shows that the performance so far in 2023 of non-dividend paying stocks has surpassed the performance of dividend-paying stocks, both for the S&P 500 in general as well as for each sector.

Figure #7 Tough Year for Stocks of Companies that Pay Dividends





Source: Strategas Research

A Generative Artificial Intelligence Test Run

Our tech-savvy investment team colleague, Jon, asked ChatGPT, a generative AI program developed by Microsoft, "Why should I invest in stocks of dividend-paying companies?". Here is what we consider to be a pretty amazing response. . .complete with a disclaimer! But don't worry. Your Dearborn Partners investment team remains committed to using human intelligence to run our Rising Dividend Strategy.

> "Investing in dividend-paying stocks can be beneficial for several reasons:
>
> 1. Steady Income Stream: Dividend-paying stocks provide a regular income stream. As a shareholder, you receive periodic cash distributions from the company in the form of dividends. This can be particularly appealing for investors who rely on income from their investments, such as retirees or individuals seeking passive income.
> 2. Potential for Growth: Dividend-paying stocks can still offer potential for capital appreciation. While some companies may prioritize dividend payments, they can still experience growth and increase their stock price over time. By investing in these stocks, you have the opportunity to benefit from both dividend income and capital gains.
> 3. Compounding Effect: Reinvesting dividends can accelerate your wealth accumulation through the power of compounding. When you reinvest dividends by purchasing more shares of the dividend-paying stock, you effectively increase your ownership in the company. Over time, this reinvestment can lead to a larger dividend income stream as well as potential capital appreciation.
> 4. Stability and Defensive Qualities: Dividend-paying stocks, particularly those from established companies with a history of consistent dividend payments, often exhibit stability and defensive qualities. Even during market downturns, these stocks may be more resilient compared to non-dividend-paying stocks, as the dividend income can provide a cushion against potential losses.
> 5. Dividends as an Indicator of Company Health: Companies that consistently pay dividends are typically financially stable and generate consistent cash flows. A track record of regular dividend payments can indicate a company's underlying strength, profitability, and commitment to shareholders. Dividend payments are often seen as a sign of management's confidence in the company's future prospects.
> 6. Diversification and Risk Mitigation: Including dividend-paying stocks in your investment portfolio can enhance diversification. Dividends can come from various sectors and industries, allowing you to spread your investment risk across different companies. By diversifying, you reduce the impact of any single stock's performance on your overall portfolio.
>
> It's important to note that dividend-paying stocks may not be suitable for all investors. Factors such as your financial goals, risk tolerance, and investment horizon should be considered before making any investment decisions. Additionally, it's advisable to conduct thorough research, analyze the financial health of the companies, and seek professional advice to make informed investment choices."

Source: ChatGPT, response to "Why should I invest in dividend paying stocks?," May 24, 2023, OpenAI.

Dividend Record

Ned Davis Research has divided the equal-weight S&P 500 into categories by dividend policy going back to January 31, 1973. Companies that have consistently increased dividends have generated the best total returns, whereas companies that have cut or suspended dividends have generated the worst total returns. A primary objective of our Dearborn Partners Rising Dividend Strategy is to include in our portfolios only companies for which we have a high degree of confidence in their ability to consistently increase dividends and to avoid companies whose dividends may not be secure.

S&P Dow Jones Indices compiles records of companies in the S&P 500 that have changed their dividend rates: how many companies increased dividends, how many initiated a dividend, how many decreased and suspended their dividends. Looking at this decade, beginning with 2020—when the novel coronavirus first emerged, there were no vaccines yet, and businesses were divided into essential and nonessential, with nonessentials being closed—fewer companies increased their dividends and more companies decreased dividends than any year since the Global Financial Crisis in 2008-2009, and more companies suspended their dividends than any year since S&P began keeping these records in 2004.

	INCREASES	INITIALS	DECREASES	SUSPENSIONS
YTD 2023	189	5	12	4
2022	377	7	5	0
2021	353	19	4	1
2020	287	11	27	42

Source: S&P Dow Jones Indices, S&P 500 Issue Indicated Dividend Rate Change

Business conditions settled down in 2021 and 2022 so that more companies resumed dividend increases and far fewer companies cut or suspended their dividends. Perhaps the Federal Reserve's interest rate actions are having an effect on some businesses, however, because so far this year, the number of companies cutting and suspending dividends has picked up again. **No companies in our Dearborn Partners Rising Dividend separately managed account (SMA) portfolios, however, have cut or suspended dividends so far this year.**

Here are some details about the dividend increases announced by the companies in our separately managed accounts in the second quarter of 2023.

Dividend Growth: Core Rising Dividend SMA portfolio

In the second quarter of 2023, 6 of the 49 companies in our Core Rising Dividend portfolio announced 6 dividend increases averaging about 10.1% more than those companies paid a year earlier. In the first half of 2023, 22 of 49 companies announced 22 dividend increases averaging about 7.8% more than those companies paid a year earlier. One company declared a special dividend in the first half of this year.

Dividend Growth: High & Rising Dividend SMA portfolio

In the second quarter of 2023, 4 of 25 companies in our High & Rising Dividend portfolio announced 4 dividend increases averaging about 2.65% more than those companies paid as dividends a year earlier. In the first half of 2023, 14 of 25 companies announced 16 dividend increases averaging about 6.1% more than those companies paid a year earlier. One company announced a dividend increase after only two months and another increase after only one month. One company announced a dividend increase after only one quarter.

Cumulative Income Summary

Here is the cumulative dividend income generated by the shares held in companies in both of our Dearborn Partners Rising Dividend SMA Portfolios from two actual accounts, each with an initial $200,000 investment on September 30, 2011 (the inception date of our SMA portfolios) through June 30, 2023:

	Average Current Yield	Cumulative Income*
Core Rising Dividend SMA	2.0%	$118,122
High & Rising Dividend SMA	3.3%	$159,857
S&P 500	1.5%	$103,098

**The S&P 500 dividend income in the table above is calculated by creating investable "share units" by dividing an actual $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 June 30, 2023.*

The table above shows that the average yield of both of our Rising Dividend SMA portfolios at the end of the second quarter of 2023 exceeded the average yield of the S&P 500. As a result of their above average yields, lower volatility, and generally conservative features, our portfolios may appeal to some generally risk-averse investors who are in search of yields greater than those offered by the broad market.

Dearborn Partners' Rising Dividend Philosophy

The Dearborn Partners Rising Dividend investment team works very hard to try to find companies that we consider capable of increasing dividends at rates that help investors keep ahead of the rising costs of living throughout any kind of environment—economic, interest rate, political, social, taxation, unprecedented pandemics, severe weather, war, peace, etc. Some of the eleven sectors into which Standard & Poor's divides the marketplace are more economically sensitive than others. From every sector, however, we look for what we consider to be the most defensive—i.e., consumers patronize their products or services in tough economic times as well as good times—and now the most essential businesses with strong balance sheets, high barriers to entry, and solid management.

This year, many market strategists or prognosticators predicted a poor stock market and encouraged waiting in U.S. Treasury bills until more favorable market conditions develop. Consider what their followers missed: the S&P 500's total return in the first half of 2023 was +16.9%. It's true that short-term U.S. Treasury bill yields are finally offering rates that provide decent alternatives to stocks, including stocks of companies offering attractive dividend yields. As we write this, the 6-month U.S. Treasury bill yields 5.4%. For the first time since before the Global Financial Crisis in 2008, savers are no longer being punished and securities with the full faith and credit backing of the United States government can provide decent returns risk free and thus viable diversification to portfolios. Remember, however, that U.S. Treasury instruments offer no growth. The Federal Reserve is signaling that they plan to continue to raise the Fed Funds Rate at more upcoming meetings. If so, when current 6-month bills mature, rolling into the next ones could make sense for a while. But once the Fed believes that inflation is under control, or the economy enters a recession, interest rates may decline. In other words, we make no market forecasts; instead, we continue to believe that owning well-diversified portfolios of high-quality companies that offer the potential to consistently increase dividends over time makes sense as a core component of investors' portfolios.

As we know, companies don't grow overnight; growth takes years and investors must be patient. We insist that every company pays dividends. In fact, we insist that the dividends represent a prudent percentage of earnings and cash flow so that the companies can reinvest most of the cash generated for future growth of revenues, cash flow, earnings, and dividends. Historically, stock prices move as the earnings of the underlying company move. If the earnings and dividends can march upward over time, so should the stock prices and provide attractive total returns over the long term. We think our strategy of paying investors while waiting, and consistently getting pay raises through dividend increases should, we hope, give investors the fortitude to stay invested throughout any environment.

The lens through which we examine every company in our portfolios and those that may be candidates for our portfolios is: do they possess the ability to not only pay a dividend but increase the dividend consistently over time. Our view is: A dividend is tangible evidence of a company's health; a rising dividend telegraphs a company's strength.

We are truly grateful that you are taking this journey with us and hope that you will patiently stay with us for many years to come. That we concentrate so intently on including in our portfolios companies that offer the potential to continuously pay and increase dividends we hope will enable you to get invested and stay invested in our equity portfolios throughout the volatility and in any environment. We promise to continue to work hard to try to bring you lots of rising dividends.

The Dearborn Partners Investment Team
Carol, Mike, Pete, Matt, and Jon

Dearborn Partners Rising Dividend Separately Managed Account Average Calendar Year Dividend Increases[1]

	Core Rising	High & Rising	CPI*
11-Year Average	10.4%	7.6%	2.6%
YTD 2023	7.8%	6.1%	5.3%
2022	11.8%	8.7%	6.0%
2021	9.9%	6.3%	5.5%
2020	7.6%	5.9%	1.6%
2019	9.6%	8.2%	2.3%
2018	12.9%	8.8%	2.2%
2017	7.8%	5.8%	1.7%
2016	8.0%	6.5%	2.1%
2015	9.7%	7.5%	2.1%
2014	12.2%	7.4%	1.6%
2013	12.2%	8.7%	1.7%
2012	13.0%	9.6%	1.9%

** Core Consumer Price Index for All Urban Consumers Unadjusted 12-month Percent Change for 12 months ending May 2023 Updated June 13, 2023. 11-Year Average represents December 2012-December 2022. YTD = Year to Date*

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 June 13, 2023.

[1] 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.

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