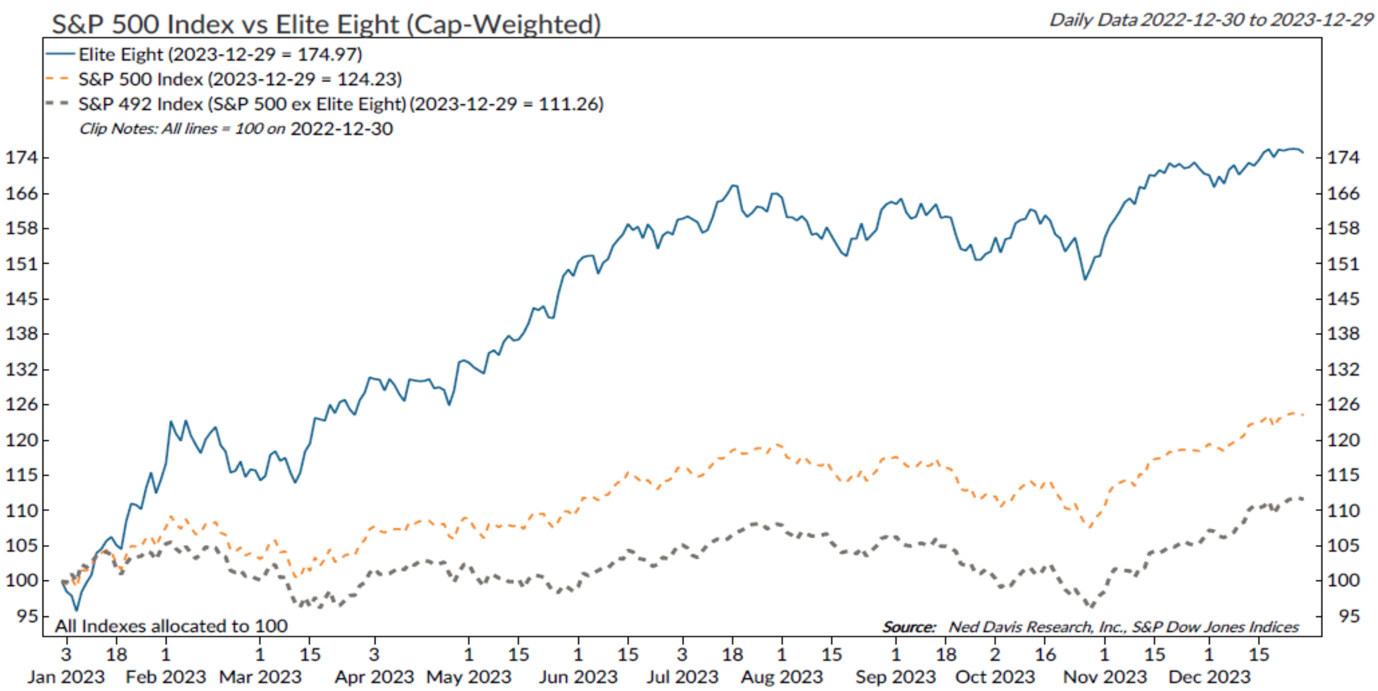
DEARBORN
PARTNERS

<u>Year End 2023 Commentary</u> **Carol M. Lippman, CFA**

The Stock Market Remains Heavily Concentrated

Ned Davis Research wrote: "S&P 500 is masking another tough year to find winners. The reason is that the small percentage of stocks outperforming includes mega cap Growth names. Our Elite Eight Index (the solid blue line in Figure #1) soared 75% in 2023. Excluding the Elite Eight (the broken grey line), the S&P 500 was up 11.3%. Diversifying via asset classes and within equities has been a challenging strategy in 2023."

Figure #1: Nearly all the gains in the S&P 500 Were from the Elite Eight



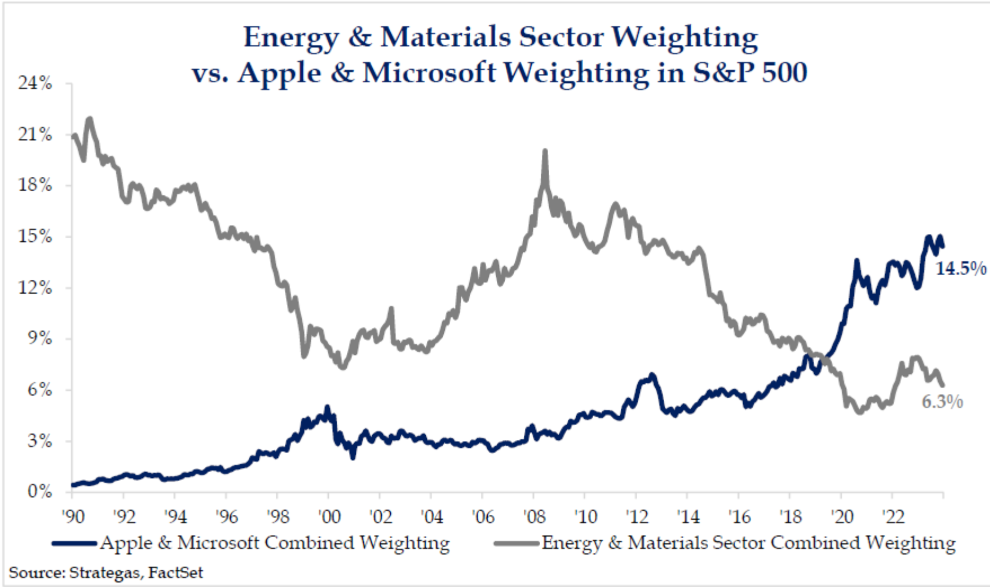
Ticker	Name
META	Meta (Facebook)
AMZN	Amazon.com
NFLX	Netflix
MSFT	Microsoft
AAPL	Apple
GOOGL	Alphabet
TSLA	Tesla
NVDA	Nvidia

Index (Cap-Weighted)	Gain/Annum % 2022-12-30 to 2023-12-29	YTD % 2022-12-30 to 2023-12-29
Elite Eight	75.24	74.97
S&P 500 Index	24.30	24.23
S&P 492 Index (S&P 500 ex Elite Eight)	11.29	11.26

The challenge for most active portfolio managers is that prudently diversified portfolios typically draw heavily from the 492 securities in the broad market. When the returns of the benchmark do not reflect broad participation, it is difficult for properly diversified portfolios to keep up.

Strategas Research presented more evidence of concentrated market dominance with this illustration showing that the capitalization weights of two stocks in the S&P 500—Apple and Microsoft—as of December 31, 2023 exceed the weightings of two entire "real economy" sectors—Energy and Materials.

Figure #2: Strategas: "Real Economy Sectors Pale in Comparison to Growth Index Behemoths. . ."



Source: Strategas Research—Quarterly Review in Charts

Apple and Microsoft are the only two companies in the Elite Eight that pay dividends that have increased year after year: Apple's beginning in August 2012 and Microsoft's beginning in February 2003.

S&P 500 Dividends Had Challenges in 2023

As might be expected—given that much of the world and many businesses deemed non-essential were shut down beginning in early 2020 when the novel Corona virus emerged and before vaccines and adequate treatments were invented—many companies had difficulty maintaining and increasing dividends relative to previous years. Normal dividend growth generally resumed in 2021 and 2022. In 2023, however, more companies cut and suspended dividends than any years since 2020 and The Great Financial Crisis in 2008-2009.

Figure #3: S&P 500 Indicated Dividend Rate Change as of 12/29/2023

	INCREASES	INITIALS	DECREASES	SUSPENSIONS
2023	348	11	26	4
2022	377	7	5	0
2021	353	19	4	1
2020	287	11	27	42
2019	355	6	7	0
2018	374	6	3	0
2017	351	5	9	2
2016	344	7	19	2
2015	344	7	16	3
2014	375	8	8	0
2013	366	15	12	0
2012	333	15	11	1
2011	320	22	5	0
2010	243	13	4	1
2009	151	6	68	10
2008	236	5	40	22

Source: S&P Dow Jones Indices 12/29/2023 S&P 500 Issue Indicated Dividend Rate Change
403 issues (80.1%) with an S&P indicated dividend rate, 76.7% of the market value

The companies in our Dearborn Partners High & Rising Dividend portfolio, on the other hand, have on average continued to increase dividends at rates in accordance with our stated objective of mid-single-digit annual growth. Here are some details about the dividend increases announced by the companies in our separately managed account (SMA) in the fourth quarter and full year 2023.

Dividend Growth: High & Rising Dividend SMA portfolio

In the fourth quarter of 2023, 9 of 25 companies in our High & Rising Dividend portfolio announced 9 dividend increases averaging about 7.7% more than those companies paid as dividends a year earlier. In full year 2023, 24 of 25 companies announced 28 dividend increases averaging about 6.9% more than those companies paid a year earlier. One company announced a dividend increase in February after only two months, then another increase only one month later in March, and increases each quarter thereafter. No companies in this portfolio reduced or suspended dividends in 2023.

Update of Performance by Dividend Category

Despite the challenges 2023 presented for dividends for many companies as well as for the performance of the stocks of companies not in the Elite Eight in the S&P 500, over longer time periods, dividends have helped the performance of investment portfolios. In last quarter's Commentary, we showed Ned Davis Research's performance by dividend category for several time periods: full years 2020 through 2021 and 2022. Figures #4-#6 are from Ned Davis Research. Source: *Copyright 2024 Ned Davis Research, Inc. Further distribution prohibited without prior permission. All Rights Reserved. See NDR Disclaimer at www.ndr.com/copyright.html. For data vendor disclaimers refer to www.ndr.com/vendorinfo/.*

As seen in Figure #4, returns for all dividend categories were generally strong in full years 2020 and 2021. Non-dividend paying stocks generated the best returns. In 2022, the market capitalization-weighted S&P 500 Index registered the textbook definition of a bear market: down -20%, the total return of the equal-weighted S&P 500 Index, which Ned Davis uses in these studies, declined -14.8%, and non-dividend paying stocks, the worst performing category, were down about 30%. The top two categories of dividends, did not generate the best returns in either of these periods but generally lost less in 2022 than three of the other categories.

Figure #4 **2020-2021 Total Returns**

Portfolio Performance Statistics Analysis Dates: 2019-12-31 - 2021-12-31		
Portfolio	Gain/Annum %	Growth of $100
Dividend Growers & Initiators	13.8	129.5
All Dividend-Paying Stocks	14.6	131.5
Dividend Payers w/No Change in Dividends	12.6	126.8
Dividend Cutters & Eliminators	11.1	123.5
Non-Dividend Paying Stocks	17.6	138.4
S&P 500 Geometric Equal-Weighted Total Return	15.1	132.6

2022 Total Returns

Portfolio Performance Statistics Analysis Dates: 2021-12-31 - 2022-12-31		
Portfolio	Gain/Annum %	Growth of $100
Dividend Growers & Initiators	-9.3	90.7
All Dividend-Paying Stocks	-9.9	90.1
Dividend Payers w/No Change in Dividends	-14.5	85.5
Dividend Cutters & Eliminators	-7.1	92.9
Non-Dividend Paying Stocks	-29.9	70.1
S&P 500 Geometric Equal-Weighted Total Return	-14.8	85.2

In 2023, as seen in Figure #5, the equal-weighted broad market index's total return was 10.7% and non-dividend payers bounced back a strong +21.6%. Even though most stocks turned in solid returns in 2023, with only dividend cutters and eliminators still losing money, Figure #6 shows that for the entire four-year period from 2020 through 2023, the top two dividend categories provided the best total returns.

Figure #5 **2023 Total Returns**

Portfolio Performance Statistics Analysis Dates: 2022-12-31 - 2023-12-31		
Portfolio	Gain/Annum %	Growth of $100
Dividend Growers & Initiators	8.1	108.1
All Dividend-Paying Stocks	8.6	108.6
Dividend Payers w/No Change in Dividends	14.2	114.2
Dividend Cutters & Eliminators	-1.9	98.1
Non-Dividend Paying Stocks	21.6	121.6
S&P 500 Geometric Equal-Weighted Total Return	10.7	110.7

Figure #6 **2020-2023 Total Returns**

Portfolio Performance Statistics Analysis Dates: 2019-12-31 - 2023-12-31		
Portfolio	Gain/Annum %	Growth of $100
Dividend Growers & Initiators	6.1	127.0
All Dividend-Paying Stocks	6.5	128.7
Dividend Payers w/No Change in Dividends	5.5	123.9
Dividend Cutters & Eliminators	3.0	112.6
Non-Dividend Paying Stocks	4.2	117.9
S&P 500 Geometric Equal-Weighted Total Return	5.7	125.1

What lessons can we draw from this Ned Davis Research by dividend category?

- If investors can lose less money in bad markets, it is not necessary to work as hard to try to recover big losses.
- Slow and steady can win the race.
- Companies with the ability to consistently pay and increase dividends are typically of good quality. Staying invested for many years in well-diversified portfolios of stocks of good quality companies, patiently participating in the market while collecting dividends with the potential to increase with regularity, has generally rewarded investors.

The Dearborn Partners investment team adheres to these time-tested themes. We do not make predictions about the direction of markets or interest rates or other macroeconomic factors. We do not try to time when to get into or out of stocks. We constantly work hard trying to find for our portfolios good quality companies that we consider capable of increasing dividends year after year. We strive to offer a palatable strategy that allows investors to get in the market and stay in the market.

This Quarter's Generative Artificial Intelligence (AI) Test Run

This quarter we asked ChatGPT, a generative AI program developed by Microsoft, "Why does a company pay a dividend?" Here is the response, once again complete with a disclaimer.

> "A company pays a dividend as a way to distribute a portion of its earnings or profits to its shareholders. This distribution is typically in the form of cash, although it can also be in the form of additional shares or other property.
>
> Here are some reasons why a company may choose to pay dividends:
> 1. **Rewarding Shareholders**: Dividends are a way for a company to reward its shareholders for investing in the company. It provides a return on their investment and can attract more investors.

2. **Attracting Investors**: Paying consistent and attractive dividends can make a company more appealing to income-seeking investors, such as retirees or those looking for regular income from their investments.
3. **Signal of Financial Health**: A company that pays dividends regularly is often seen as financially stable and generating sufficient profits to distribute to shareholders. This can enhance the company's reputation and attract more investors.
4. **Tax Efficiency**: In some jurisdictions, dividends may be taxed at a lower rate than other forms of income, making them an attractive way for shareholders to receive a return on their investment.
5. **Utilizing Excess Cash**: If a company has excess cash that is not immediately needed for growth or reinvestment, it can use this cash to pay dividends to shareholders.
6. **Maintaining Investor Confidence**: Companies that have a history of paying dividends and continue to do so even during challenging economic times may maintain investor confidence and demonstrate a commitment to shareholder value.
7. **Steady Income Stream**: Dividends provide shareholders with a steady income stream, especially those who rely on their investments for living expenses.

It's important to note that not all companies pay dividends. Some companies may choose to reinvest all their profits back into the business for growth, acquisitions, debt reduction, or research and development rather than distributing them to shareholders. The decision to pay dividends is influenced by a company's financial situation, growth prospects, industry trends, and overall strategic objectives."[1]

We on the Dearborn Partners investment team try to analyze the companies for our portfolios so well before adding them that we hope to be able to own them "forever." In fact, our average turnover is very low: less than 12% annualized since inception. Sometimes, however, companies lose their disciplines or unforeseen developments change the dividend's position relative to other important fundamentals. Our discipline emphasizes assessing our view of a company's ability to not just maintain a dividend but to be able to increase it with regularity and consistency. We believe that enforcing such a strict criterion provides for removing a company before the security of the dividend becomes a concern.

Cumulative Income Summary

Here is the cumulative dividend income generated by the shares held in companies in our Dearborn Partners High & Rising Dividend SMA Portfolio from an actual account, with an initial $200,000 investment on September 30, 2011 (the inception date of our SMA portfolio) through December 31, 2023:

	Average Current Yield	Cumulative Income*
High & Rising Dividend SMA	3.3%	$171,092
S&P 500	1.5%	$109,387

**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 December 31, 2023.*

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

[1] ChatGPT, response to "Why does a company pay a dividend?" 9/19/2023, OpenAI.

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—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 developed. Consider what their followers missed: the market capitalization-weighted S&P 500's total return for the year ended December 31, 2023 was +26.3%, the equal-weighted S&P 500's total return was +10.7%, about in line with that benchmark's average annual total return since 1925 of 10%. It's true that short-term U.S. Treasury bill yields are finally offering rates that provide decent alternatives to stocks of companies that offer attractive dividend yields. As of December 31, 2023, the 6-month U.S. Treasury bill yield was 5.24%. 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 may cut the Fed Funds Rate at upcoming meetings. If so, when current 6-month bills mature, rolling into the next ones may provide lower yields. 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]

	High & Rising	CPI*
12-Year Average	7.5%	2.7%
2023	6.9%	4.0%
2022	8.7%	6.0%
2021	6.3%	5.5%
2020	5.9%	1.6%
2019	8.2%	2.3%
2018	8.8%	2.2%
2017	5.8%	1.7%
2016	6.5%	2.1%
2015	7.5%	2.1%
2014	7.4%	1.6%
2013	8.7%	1.7%
2012	9.6%	1.9%

** Core Consumer Price Index for All Urban Consumers Unadjusted 12-month Percent Change for 12 months ending November 2023 Updated Dec. 12, 2023. 12-Year Average represents December 2012-December 2023.*

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 September 13, 2023.

[1] On the date that a company in our SMA portfolio 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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