April 18, 2023

Dear Clients and Friends:

Re: Q1 Investment Review

As shown below, the first quarter of 2023 continued the "interesting times" that the stock and bond markets have now been experiencing since the end of 2021 when the S&P 500 peaked at about 4800. Following some recovery over the past two quarters, it closed the first quarter of this year around 4170, still well below the high-water mark.

Benchmark Index Total Returns	Quarter Ending 3/31/2023	Year Ending 3/31/2023
Lipper Balanced Fund Index	4.30%	-6.00%
S&P Dividend Aristocrats	1.80%	-1.55%
S&P 500 Stock Index	7.50%	-7.73%
Russell 1000 Value Index	1.01%	-5.91%
3-month US Treas. Bill Index	1.11%	2.50%
S&P-7-10 Year US Treas. Bond Index	3.92%	-5.65%
S&P U.S. Gov & Corporate 30 Year Bond Index	6.70%	-20.19%

Over the past several years, the U.S. and global economies have been dominated by the COVID epidemic. Because of COVID, very large relief programs were initiated by the government to reduce the economic impact of the disease. As demand was kept in check by lockdowns and other restrictions, ample cheap money and federal stimulus did their jobs to keep the economy moving forward. But nothing is free in the world of economics. Eventually, too much demand due to overspending by the Federal government in the presence of COVID constrained supply along with too much money brought about the inflation we are now seeing.

Over time, trillion-dollar Federal deficits do matter, in spite of some new economic theories of growth and inflation that were used to justify spending. We hope these have now been discredited as some

rules never change. With hindsight, it is clear that there was just too much economic stimulation. The definition of inflation is the creation of too much demand in the presence of too much money.

Higher inflation virtually always results in higher interest rates as the Federal Reserve tries to constrain money growth to bring price increases back under control. And higher interest rates leading to recession generally produce lower stock prices. In spite of the recent stock market rally, that is where we believe we are now.

In the very imperfect process of trying to "manage" economic growth with low inflation there are no perfect solutions. Today everyone is arguing about what should have been done differently, but after the fact solutions are always clear cut. Peering into the future is what is difficult. Virtually no one is consistently correct, and the consensus is almost always way off the mark.

In spite of this, the quarter just ended did do pretty well for itself in stock market terms. After a strong January rebound, February was a loser but then there was a comeback in March led by beaten down Tech stocks, with the general market returning about 7% year to date. The fourth quarter of 2022 also did well, so some ebullience is now working its way back into investor attitudes. If we annualize the recent quarter, it implies that 2023 will produce a 28% return. We don't think so.

Based on the current numbers, another increase in interest rates is highly likely when the Fed next meets in May, but there is no question that we are much closer to the end of rate increases than the beginning. So far, the indications that the economy and inflation will continue to cool are limited, though progress has been made.

With much anticipation already built into current stock prices, a pullback of some degree is very likely, especially if we get some bad news along the way. Given all that is going on geopolitically in the world today, some bad news is quite likely. Also, company earnings reports are due to begin arriving shortly and are expected to show declines versus a year ago, and this too may start to have an impact. Add in the current debt ceiling and budget debates, and the odds of something less than smooth sailing happening do get higher.

As we have said in the past, it is not impossible to get out of our current economic problems and back on the path to growth with low inflation without recession, but we continue to think the odds are very low.

Top 20 Holdings

Our Top 20 Holdings can be found in the list below. This quarter saw Cardinal Health replaced by Stanley Black & Decker. Stanley had dropped off the list in the previous quarter due to performance and tax loss selling, and it made its way back on the list as we repurchased shares and added some new positions in the first quarter.

3/31/2023 Top Holdings

ABBV	AbbVie Inc.	LEG	Leggett & Platt Inc
AMP	Ameriprise Financial	LOW	Lowes Companies Inc

AMGN	Amgen Inc	MRK	Merck & Company Inc
ADM	Archer Daniels Midland	MSFT	Microsoft Corporation
CAT	Caterpillar Inc	PII	Polaris Industries Inc.
CSCO	Cisco Systems Inc	QCOM	Qualcomm Inc.
CMCSA	Comcast Corporation	SWK	Stanley Black & Decker
EPD	Enterprise Products Partners LP	XLK	SPDR Technology Sector ETF
FAST	Fastenal Company	TGT	Target Corporation
ITW	Illinois Tool Works Inc	TROW	T Rowe Price Group

Cardinal Health was one of our biggest winners over the last year, gaining about 40% for the year ending March 31. As one of the major players in the legal issues and lawsuits surrounding the opioid crises, the stock had previously been pummeled. In addition, Covid related logistical and sales problems led to a sales slowdown and had an inflationary impact on costs. The stock began its rebound as these issues began to be resolved. They were one of the first companies to seek settlements after the opioid problems though they were just the delivery mechanism rather than the manufacturers or prescribers.

Our selling was based on expectations of slower than historic growth and, after the appreciation, gross overvaluation of the stock price based on the company's future prospects. We are now largely out of Cardinal Health except for a few accounts where the tax consequences of selling would be too high. The current dividend yield of around 2.5%, while not bad, is well below where the stock has historically traded. Putting it all together, Cardinal Health was a great stock to own over the last few years, and it was an easy decision to sell it in order to take advantage of better opportunities.

We believe one of those opportunities is Stanley Black & Decker which dropped off our top holdings list in the last quarter. The company is the dominant player in the manual and power tools industries and number one or two in all of its major industries, but business has been tough recently. Stanley operates in a cyclical industry that is currently at or near a low in its market cycle. However, as we look closer at the company, we like what we see.

Stanley has paid consecutive dividends for 146 years, the best of any industrial company on the New York Stock Exchange. Additionally, the company has raised the dividend for each of the last 55 years. Meanwhile, the fundamentals look good with reasonable debt levels and a dividend that remains well covered. The company will be in recovery mode this year as it works to cut costs, but this, and general economic recovery, are expected to produce a big rebound in earnings in 2024. Stock prices are forward looking, and we believe this is a stock that could soar once it looks like the wheels of a recovery are in motion. Additionally, the current dividend yield for Stanley is about 4.3%. If we sell Cardinal Health today in order to buy Stanley Black & Decker, we are picking up a big increase in income as well as improved capital gain potential. This is the kind of trade we look for all the time.

Throughout the first quarter we have continued to reduce or sell many of our winners in addition to Cardinal Health, such as Archer-Daniels-Midland and Abbvie. In many cases, they had just become too

large a position in many portfolios. And we are finding plenty of stocks to choose from for purchase, which is not always the case. We continued adding to high quality names like Target and T. Rowe Price over the quarter. We also added real estate holdings including Essex Property Trust and Digital Realty. And more recently we have been taking a close look at our bank holdings. We believe our top bank holdings, including Truist, US Bancorp, JP Morgan and Bank of New York Melon, all remain very high-quality companies that are not at any material risk of failure or disruption, and we have begun to add to some of these positions as prices declined in sympathy to the Silicon Valley Bank debacle.

Risk

Silicon Valley Bank has dominated the financial news over the past month or so. As much has already been written we will be brief but do want to make a point.

The failure of SVB was due to several factors: The regulators (Federal Reserve Bank of San Francisco) knew there were some issues but did nothing about them, reaffirming our distrust of the ability of the Federal bureaucracy to keep on top of problems; very poor management judgement on investing their assets beyond what was needed for lending purposes; and also the failure of public accounting firms not to recognize the interim price risk present in their U.S. Treasury holdings.

At the end of last year, we reported that long-term U.S. Treasury securities had lost about a third of their value over the course of the year as interest rates pushed higher. While Treasuries are very safe if held to maturity, this is a great example of what can happen on a short-term basis. With inflation expectations rising for some time, we don't understand why anyone would want to own long-term bonds over this period – we certainly didn't.

When large deposits began to be withdrawn from the bank, as loans are difficult to liquidate, they were forced to sell these bonds at large losses and eventually ran out of liquidity that led to the bank failure.

Interestingly, in addition to the Federal Reserve Bank miss, the SVB stock was also followed and researched by a substantial number of common stock analysts, both broker related and independent. Most of them missed the problems too, as the stock was almost universally rated a "Buy".

The point of this discussion is that this sort of thing can happen almost anywhere in the financial markets due to unanticipated problems. In this case, a review of the balance sheet by any bank analyst paying close attention would have revealed these issues.

The first thing we do before buying anything for clients is to look at the financial strength and limit ourselves to the purchase of only top-quality companies. While Silicon Valley Bank was the 16th largest in the country by deposits held, it was never in the top tier in terms of quality.

Owning only the highest quality companies may lead to lagging performance when everything seems to be going great, but it more than pays off when times get tough. This is why we have not been shaken out of Stanley Black & Decker, though with hindsight we clearly bought it too early. And that is why we have the confidence to buy more at today's "sale" price even though recent results have been poor. In the long-run, quality pays off and a low entry price only adds to the attractiveness of what we buy.

Performance Comparisons

As you review your performance numbers attached to your asset appraisal, you may notice we provide four different indexes for comparative purposes. Occasionally you come out ahead of all of them but most of the time we are ahead of the performance of two or three. The reason is that each measures a different dimension of performance. There is no one single "best" measure.

The S&P 500, for instance, measures the total change in market value of all the stocks in the index and because of that is considered the best aggregate measure of "the stock market". The shortcoming of this approach is that it gives much more weight to the largest companies at the expense of the performance of smaller companies. In contrast, the Dow Jones Industrial Average, which we don't use for comparative purposes, is made up of only thirty committee selected "blue chip" stocks and is price weighted, meaning the higher the price, the larger the weight in the index calculations. Neither of these two indexes have much meaning relative to the way portfolios are actually managed.

The Dividend Aristocrats Index, in contrast, consists of only those stocks in the S&P 500 that have increased their dividends each year for 25 consecutive years. This is an elite group of companies and, unlike the two indexes above is "equal weighted", an approach to measuring performance much closer to the way portfolios are actively managed. In fact, this group of stocks is one of the first places we look when seeking high quality, well-valued new holdings. Both Cardinal Health and Stanley Black & Decker are members of the index and we would happily buy Cardinal back if the price went down far enough.

We show the Lipper Balanced Index as virtually none of our accounts are invested 100% in stocks, and this index includes cash and bonds. All the others are 100% common stocks. Finally, the Russell Value Index is calculated similarly to the S&P 500 but only captures "value stocks" as defined by Russell. This emphasizes low valuation stocks due to slower long-term growth. As our orientation is toward buying when stocks are substantially down in price, we are sometimes characterized as a "value" manager. This index captures that sector of the market.

The reason to review this is that there has been an unusual amount of dispersion in performance over the last year between the different performance measurements. The indexes generally all move in the same direction but the difference in returns in the short run can be substantial, depending on what is in or out of favor in the marketplace. With the market decline, stock buyers and sellers have been changing portfolio holdings at an unusually high rate. The favorites of two years ago (mostly large high-tech companies that pushed up the S&P returns) turned into the losers over the past year. Ultra-high valuations came back to more normal levels and the high-quality Dividend Aristocrats came much more into favor as investors sought more safety, reliability of returns and less volatility. This is also why we normally emphasize dividend aristocrat type stocks.

From our perspective, index returns are interesting but we think it is much more important to meet specific performance and cash needs rather than do better than a particular index, whichever it may be. But all clients should know how they are generally doing and that is why we provide the comparisons.

Conclusion

Given all that is going on at the moment, we think it highly likely that times will continue to be "interesting" even if sometimes uncomfortable. We do take some comfort from the high quality of our

holdings, the above average dividends that they pay and the fact that we hold very few that are grossly overvalued and therefore at risk of large or permanent price decline.

We construct portfolios that are consistent with our clients' needs rather than to "beat" the performance of a specific index. If there are times that this works to our competitive disadvantage, so be it. We were founded on the idea that your needs will always come first and this continues to be our most important guiding principle.

Sincerely,

Loudon Investment Management LLC

DML/ELS/JJS/LRO