Bahl&Gaynor
Investment Counsel

A letter from the

Bahl & Gaynor Investment Committee

In this issue:

Celebrating 30 Years of Serving You!

It is with a deep sense of gratitude and some measure of pride that we look back on 30 years of all that is Bahl & Gaynor Investment Counsel.

We have certainly evolved; from four employees in July 1990 to 54 today, and two moves to bigger office space. Along the way our hand selected investment professionals and administrative staff joined us in becoming owners, thus ensuring our firm's future and commitment to success.

From day one, Bahl & Gaynor has operated with one person in mind: YOU. We knew in 1990 that investing in dividend paying stocks which provide a growing stream of income would deliver the greatest benefit to those we serve, especially during unpredictable markets. We recognize in investments, as in life, there are many things we cannot control. Still, dividends from intelligently selected companies, tend to provide a more dependable return, which in turn assists you in more reliably attaining your goals. We remain committed to the continuity of our philosophy and the long-term financial strength it yields... for you.

We take seriously the stewardship of your funds. We thank you for the trust you've placed in Bahl & Gaynor these past three decades. We are committed to working with integrity on your specific needs for decades to come.

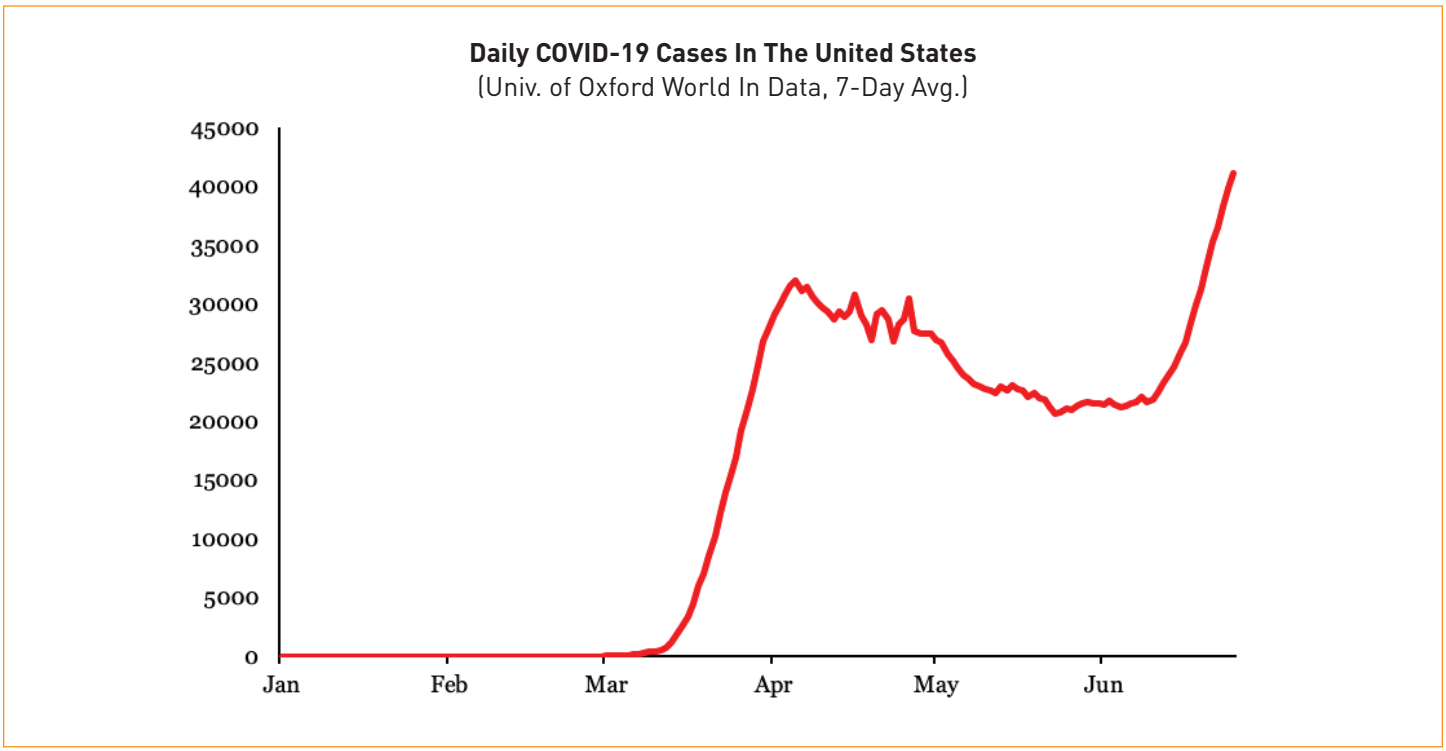
Sincerely,

Bill Bahl
Co-Founder & Chairman

Vere Gaynor
Co-Founder & President

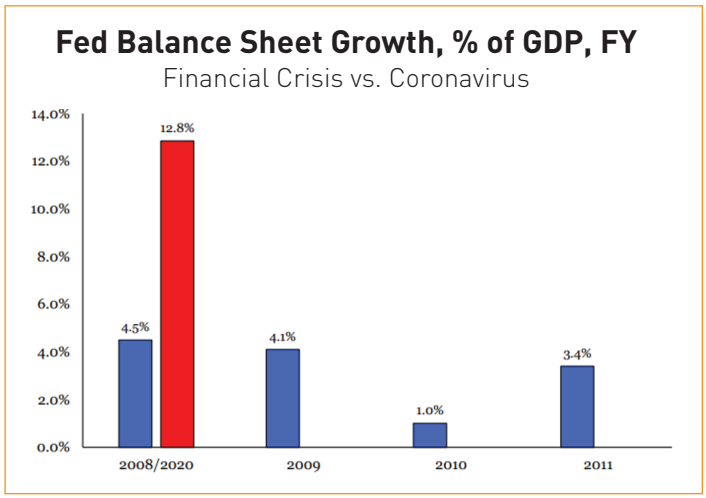
The Road to Recovery

The human tragedy and economic impact of the COVID-19 pandemic cannot be overstated. Daily impact is evident on a global scale and remains a central aspect of everyday life (see graph below). Public health-driven efforts to contain the spread of the virus slowed economic activity to such an extensive degree that GDP growth, employment markets, consumer sentiment and capital market functions suddenly reflected recessionary profiles in a matter of weeks. During the quarter, the National Bureau of Economic Research declared what capital markets had long since signaled, the US economy entered a recession in February, ending a record 128 months of consecutive economic growth since the conclusion of the Great Financial Crisis.

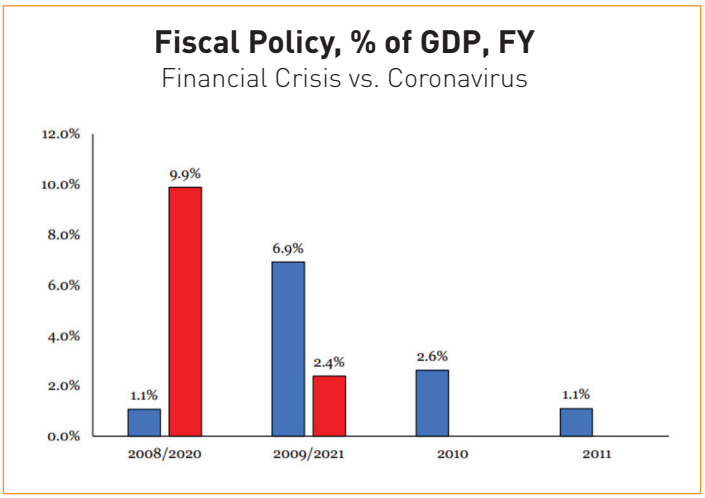


Source: Strategas, University of Oxford, 2020.

In our last quarterly note we sketched a rough outline of the monetary and fiscal efforts being formulated as that correspondence went to press. With another quarter elapsed, it appears the virtually immediate Federal Reserve and Congressional responses (pictured below) have provided a bridge, though fragile and temporary, to many individuals and businesses gravely affected by the economic disruption.



Source: Strategas, 2020.



Source: Strategas, 2020.

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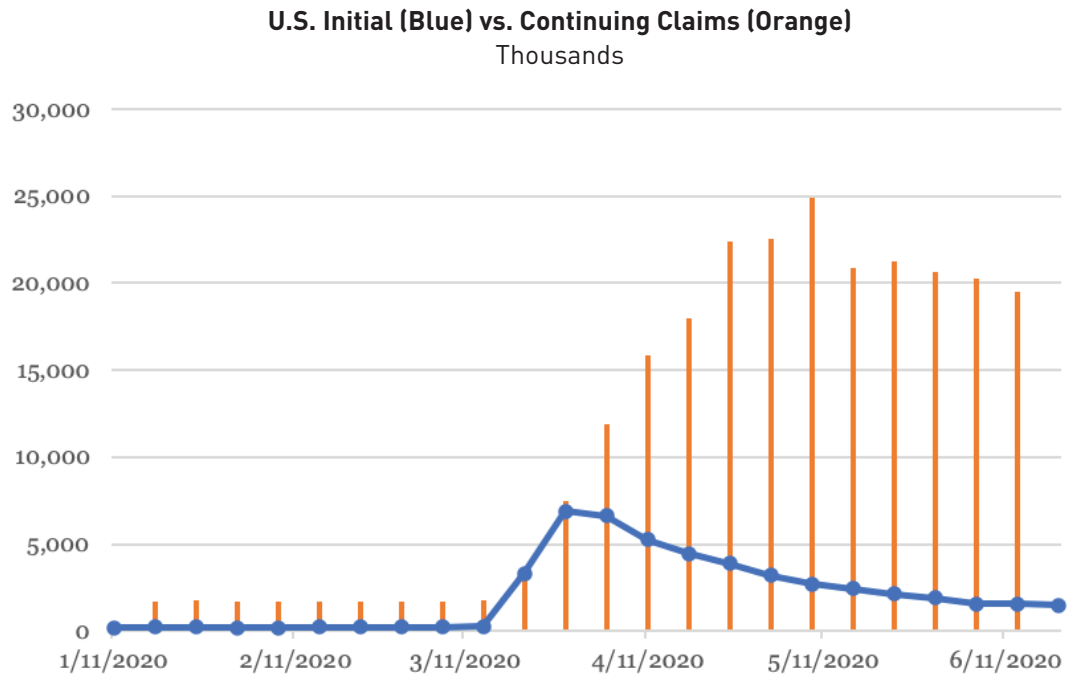
The Road to Recovery *Continued*

As we exit the second quarter, economic activity has moved forward in a constructive direction, though the degree and cadence of re-opening is uneven and driven by local infection volumes. Two key debates remain of concern to both the economy and capital markets: 1. development and approval of an effective antiviral therapy and vaccine, and 2. the ultimate "shape" of the recovery – V, U, W, L, square root, or any other iteration imaginable. No doubt the path human ingenuity takes in developing an effective medical response will greatly influence the realized shape of the recovery.

At the moment, consensus expectations seem to contemplate the development and approval of an effective antiviral and vaccine before year end 2020. However, significant manufacturing and distribution challenges remain for such therapies and likely dictates comprehensive economic activity will not return to pre-pandemic levels for several quarters, if not years. This is partly due to significant portions of the economy not reaching normal utilization patterns until an effective antiviral and vaccine response is available. Specific industries are likely to include transportation, lodging, location-based retail and entertainment and food service. It is also worth noting many of these industries involve people-intensive service delivery models, thus the employment impact of lower activity levels will represent a significant and persistent drag to economic growth. Other considerations that are more difficult to gauge include permanent behavioral changes among consumers near term and on a more permanent basis.

Macroeconomic readings in May and June that track employment (pictured below) and other important metrics have been encouraging, but incomplete, as comparisons against ghastly March and April figures mostly highlight the severity of the economic decline, not the sustainability of activity improvement. While we are encouraged by the recent direction of many consumer and producer economic indicators, readings remain well below pre-pandemic levels. Further, the sustainability of favorable advances could be called into question should a legitimate second wave of infections inhibit broader economic re-opening plans.



Source: Department of Labor, Strategas, 2020.

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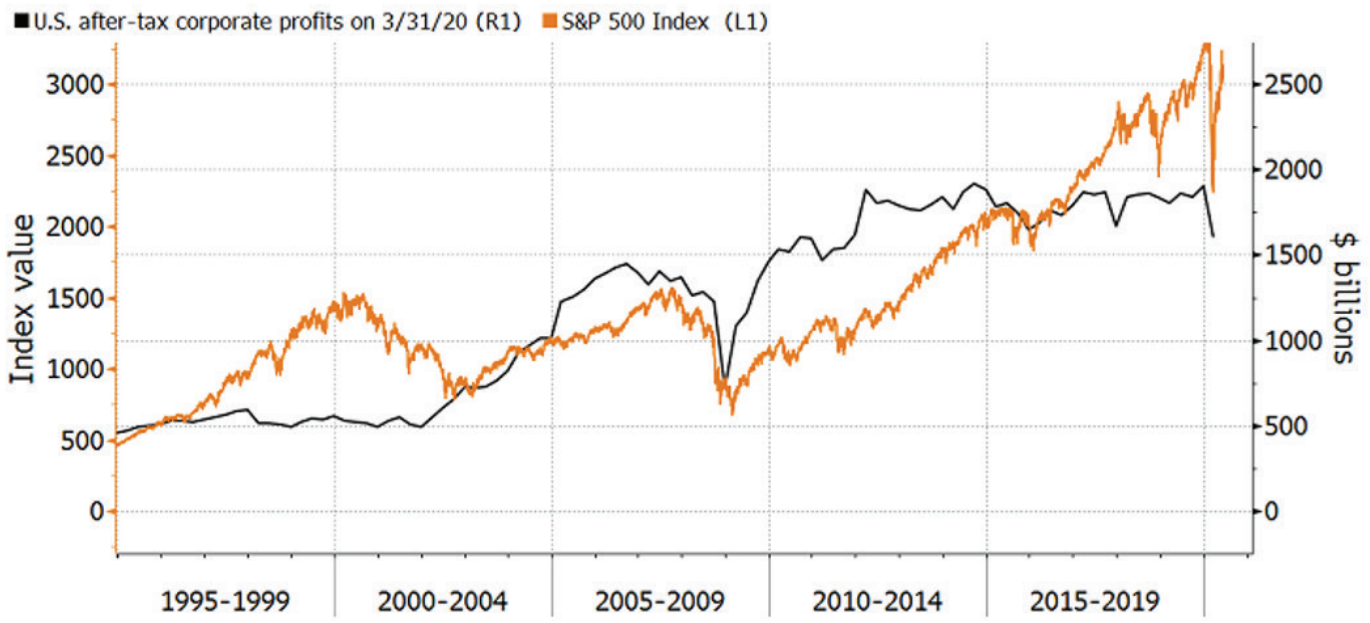
Main Street and Wall Street

The economy and capital markets are related, but not necessarily conjoined (see graph below). Economic activity and capital market direction do not always move in tandem. That is why the "Main Street" moniker is often used to describe economic concerns, as distinct from the "Wall Street" label, which is used to describe capital market dynamics. Relevant to both Main Street and Wall Street are some comparisons made to the Great Depression. To be sure, the effect on employment markets, business activity and capital market volatility aligns with or exceeds the Great Depression experience. Thankfully, the duration of this current episode may be considerably shorter due to an immediate, targeted and thoughtful response by fiscal and monetary authorities when compared to Great Depression history. Subject to additional evaluation, it is possible the recession declared by the NBER that began in February could conclude in May or June of this year.

Way Out of Sync

Disconnect between U.S. earnings and share prices is seen as caution signal



Source: US Commerce Department, Bloomberg, 2020.

Data detailing small business activity, continuing unemployment claims and mortgage deferrals suggest Main Street remains weak (see graph on top of next page). However, June-period evidence suggests important economic categories such as retail sales, housing activity and auto purchases have moved beyond their respective troughs and on to more favorable upward trajectories. Actions on the part of the Federal Reserve and Congress, which have included more than $4 trillion of liquidity and stimulus to consumers, businesses and the public sector, are clearly having the desired safety net intensions. Moreover, much of these funds have transmission mechanisms that are effective on a time delay. Thus, additional benefits from liquidity and stimulus provisions could be in the offing. Finally, Congress is expected to back an additional fiscal package in July to continue support in certain areas likely in need of it for a longer span of time. In sum, existing and anticipated monetary and fiscal support has provided Main Street with a crucial bridge to avoid a far deeper and longer-lasting recession, or worse, financial crisis, as was the case in the Great Depression.

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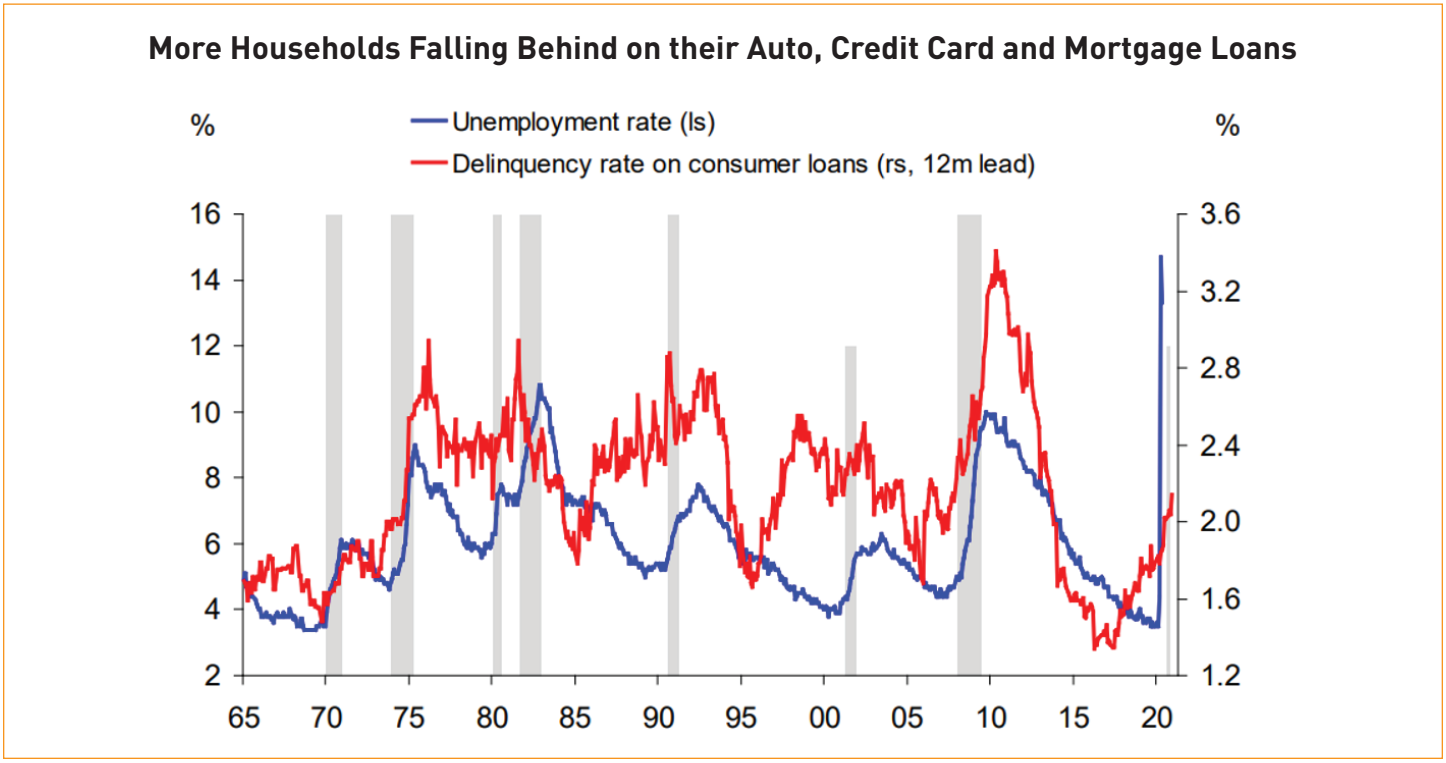

Source: BLS, ABA, Haver Analytics, Deutsche Bank Global Research, 2020.

Regarding Wall Street, the dramatic rebound in risk assets since late March is impressive and perhaps reflects an often-misunderstood driver of capital market behavior: liquidity and the discounting mechanism attendant to the market's forward-looking orientation. Although capital markets ultimately reflect the economic profile that underlies corporate profitability, short-term dynamics can be significantly influenced by factors including the cost and availability of money. The immediate availability of central bank liquidity through a veritable alphabet soup of facilities (CPFF, MMLF, PDCF, PMCCF, SMCCF, TALF, etc.) has allowed businesses to continue basic operations during a period when capital markets would have otherwise been unwilling to provide funding. Fed-driven liquidity and accompanying lower interest rates have gone a long way in comforting market participants that many of the worst-case economic scenarios resulting from the pandemic are less likely to be realized.

Ultimately these policy actions allow investors to discount current and future economic activity more favorably, thus the significant rebound in risk asset prices observed since late-March lows. But favorable trends in risk asset prices cannot be sustained on liquidity alone. Broader-based economic recovery that supports corporate profit growth is the most meaningful long-run driver of risk asset returns. While the efforts of the Fed and Congress to support economic participants through this difficult time have been heroic, it is these same economic participants that will need to take over the economic growth equation in the months ahead.

Safe Yield is Difficult to Find

Economic disruption as a result of the pandemic has pressured inflation expectations and policymakers have further intervened to push interest rates to generational lows. While low interest rates can act as a salve for businesses and risk assets as described above, they represent an increasing challenge for investors in need of income. No doubt in this low interest rate world, creditworthy borrowers have refinanced their balance sheets to lock in low-cost, long-term funding. But a 10-year commitment lending to the Treasury yields an investor little more than 0.70% annually with bank certificates of deposit and other lower-risk, market-based yields likely significantly less attractive.

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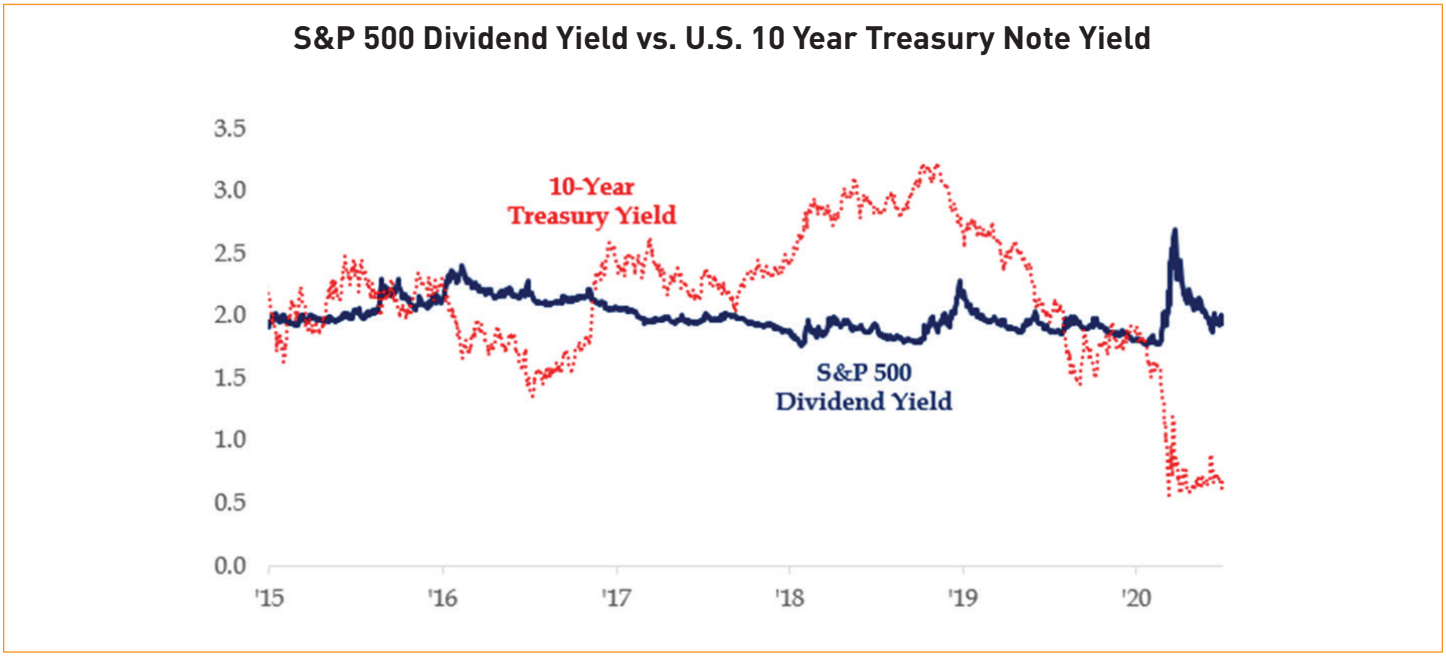
Safe Yield is Difficult to Find *Continued*

On the other end of the spectrum, seeking higher yields available in progressively riskier assets often involves concessions to quality and/or liquidity that may be outside the risk tolerance of many investors. We believe the current environment underscores the value proposition of a high-quality, dividend growth focused approach. Protection of capital from permanent loss is of great importance in a still-fluid investment environment. Thoughtful and research-based selection of common stocks with seasoned management teams, secular growth tailwinds and fundamental characteristics capable of navigating a range of recovery paths can help to guard against these capital impairment risks. Dividend yields of many common stocks exceed that of numerous fixed income alternatives (see graph below) and offer the potential for dividend growth into the future. We believe that combining these two advantages of a dividend growth strategy continues to offer the potential for attractive risk-adjusted returns in the context of a full market cycle.



Source: BLS, ABA, Haver Analytics, Deutsche Bank Global Research, 2020.

Conclusion

The COVID-19 pandemic brings unprecedented challenges to most aspects of daily life. It represents an existential threat to select industries with business models highly dependent upon the free flow of people to transact economically as they wish. In many other industries, meaningful changes must be made regarding how business is conducted. In uncontemplated circumstances, new businesses and/or industries will be born out of this moment in history – indeed – necessity is the mother of invention. In each of these respects, the pandemic has highlighted the need for an active approach to portfolio management, and as the world adapts and evolves, continued positioning to reflect or anticipate impactful changes to the investment environment. We believe our time-tested approach is as relevant today as it has been throughout the course of three decades of service to our clients.

Disclosure:

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Pandemic Era Estate Planning

It's Time to Consider Your Legacy

It used to be easier to procrastinate. Estate planning can be difficult under the best of circumstances; no one likes to ponder death. Our current health crisis makes it all too clear that life is fragile, and we are not always given the luxury of time.

Putting a thoughtful plan in place helps to ensure your wishes are carried out and, perhaps most important, eases the burden on loved ones. Without a plan in place, loved ones already will be managing a major life disruption and don't need the added anxiety of making unexpected health and financial decisions.

The elderly, those with underlying conditions, and frontline heroes are not the only individuals for whom estate planning is now absolutely necessary. The truth is, everyone benefits from creating a customized plan, which begins as a discussion with trusted legal counsel. Considerations can include, but are not limited to:

1. Defining the 'estate'

Constructing a detailed inventory of all assets and liabilities including assets that would be excluded from the estate is often the starting point of legacy planning. In this process, it is helpful to define all sources of income and future bill payments. Also, consolidating all account numbers, passwords, copies of important documents as well as names and contact information of trusted advisers in a secure, central location (digital or physical) allows for efficient accessibility after death.

2. Considering family needs

Perhaps the hardest part of estate planning is considering how loved ones will be cared for when we pass away.

- This is usually a good time to explore life insurance needs and the amount of coverage desired. Whether insurance should cover lifetime income or just a few specific goals (mortgage, tuition, etc.) are examples of questions that will need to be answered.
- If minors or dependent adults are involved, guardians should be identified and properly documented as well.

3. Identifying decision-makers

Estate plans typically include several powers of attorney (POA) designations that put another individual in charge of specific financial and medical situations in the event of your incapacity. POAs are legally powerful documents, so it is recommended that different trusted individuals be chosen for separate and distinct decision-making capacities in order to avoid overwhelming or over-empowering a single individual.

- To prevent the need for loved ones making decisions regarding end-of-life care, often a living will (also known as an advanced directive) is drafted.
- An executor and a trustee (if a trust is involved) who act as fiduciaries for the estate or trust also need to be chosen.

4. Decide where it all goes

Individuals often desire transferring (after death) assets without the burden of additional expenses and taxes or the public nature of our probate court system. In order to best avoid these unwanted outcomes, all proper legal documentation needs to be drafted, reviewed and updated. This includes a will, proper titling of assets, designating transfer on death and beneficiaries for all financial accounts including life insurance policies, and potentially establishing a trust to shelter assets.

5. Update regularly

Just as life changes, so should estate plans. Circumstances around family relationships, finances, and laws are constantly changing. It is important to update an estate plan routinely to ensure that the plan reflects your current wishes and needs.

Pablo Picasso once said, "only put off until tomorrow what you are willing to die having left undone." The rigors of aging and dying are hard for all of us. If you consider an estate plan, not as a morbid exercise, but as your legacy to your loved ones, the process can be made easier. Bahl & Gaynor can further simplify the process by working directly with your advisors to help create a seamless plan. To begin the process, simply contact your Portfolio Manager.