Income Growth Portfolio | Fourth Quarter 2023

Strategy Objectives

1. High current and growing income: 2.8% yield[1]; +8.4% growth in trailing 12-month (TTM) income as of 4Q2023
2. Downside protection: Competitive daily downside capture[2]
3. Price appreciation: Compelling alpha and Sharpe ratio

4Q2023 Results Relative to Strategy Objectives:

Income Growth

- The Income Growth strategy grew TTM income by +8.4%, compared to S&P 500 income growth of +6.7%, delivering on its primary objective to provide strong cash flow growth at enhanced yield.[3]
- 12 strategy holdings announced dividend hikes; average TTM increase was +7.5%, signaling continued financial health of the portfolio. The strategy remains positioned for broad-based dividend growth going into 2024.

Downside Protection

- Daily downside capture of 82.8% and upside capture of 79.5% across all S&P 500 down/up days in the quarter-to-date period ended 12/31/2023.[2]

Price Appreciation

- During 4Q2023, the strategy's dividend growth-focused mandate underperformed the S&P 500 benchmark and performed roughly in line with the investable universe of dividend payers with >2% yield.
- Year-over-year inflation rates continued to fall in support of the Fed's five-month, and counting, pause in interest rate hikes. In December, the Fed embraced a dovish tone, suggesting a cut may be the next move in rates, which propelled interest rate sensitive equities in the final days of the quarter. Real Estate and Financials sectors were beneficiaries of the Fed's softening stance and contributed positively to strategy performance vs the benchmark in 4Q2023.
- Dispersion of returns among the top seven holdings continued to grow following a year dominated by the largest market cap names. During the fourth quarter, these seven holdings contributed 34.3% of the S&P 500's 11.7% return, reflecting a significantly lower influence on the index compared to the 84.5% return contribution over the first three quarters of 2023.
- 2023 ended up being a boon for risk assets, particularly those beaten down the most in 2022; it was a mediocre year for S&P 500 dividend stocks with a yield > 2% as the market embraced a "recession delayed" mentality. Still, over the full year, the strategy outperformed its investable universe of dividend stocks with a yield >2%.
- We remain convicted in the outlook for risk-aware active managers with a focus on sustainable dividends and stable fundamentals as we enter 2024. With the current environment defined by the tightest monetary conditions in the last decade, and a historically imbalanced market backdrop, we believe companies with strong balance sheets and the ability to self-fund can outperform the market through-cycle.

4Q2023 Dividend Increases

Company	TTM % Increase	Current Yield
Abbott Laboratories (ABT)	7.8%	2.0%
AbbVie (ABBV)	4.7%	4.0%
Amgen (AMGN)	5.6%	3.1%
Automatic Data Processing (ADP)	12.0%	2.4%
Broadcom (AVGO)	14.1%	1.9%
Eli Lilly (LLY)	15.0%	0.9%
Exxon Mobil (XOM)	4.4%	3.8%
Lockheed Martin (LMT)	5.0%	2.8%
McDonald's (MCD)	9.9%	2.3%
Merck (MRK)	5.5%	2.8%
Realty Income (O)	3.2%	5.4%
US Bancorp (USB)	2.1%	4.5%

4Q2023 Trades Executed

Initiations	Eliminations
Amgen (AMGN)	Medtronic (MDT)
CME Group (CME)	
Dell Technologies (DELL)	
Increases	**Reductions**
CME Group (CME)	Abbott Laboratories (ABT)
Mondelez (MDLZ)	Broadcom (AVGO)
NextEra Energy (NEE)	Prologis (PLD)
Sempra (SRE)	RTX Corp (RTX)
Williams (WMB)	United Parcel Service (UPS)

Source: Bahl & Gaynor and FactSet, 2024.

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Portfolio Review

The Income Growth portfolio underperformed the S&P 500 Index in 4Q2023. Stock selection in Financials along with an overweight in Real Estate and underweight in Communication Services contributed positively to performance. An overweight in Consumer Staples, an underweight in Information Technology and stock selection in Industrials detracted from performance.

The largest positive drivers of current quarter performance included:

- Ownership of beaten-down, regional banks following a shift in the interest-rate narrative contributed positively to strategy performance.
- An overweight allocation to the Real Estate sector contributed positively to 4Q2023 performance. Ownership of Industrial REIT Prologis (PLD) was a benefit as macroeconomic and general business cycle indicators – including inflation, the unemployment rate and interest rate outlook – remained favorable and perhaps surprised to the upside during the quarter.
- No ownership of Communication Services companies was a benefit to strategy performance during the quarter. Mega-cap, media and services company Alphabet (GOOG/L) and many Communication Services sub-industries including cable and broadcasting underperformed the benchmark during the quarter.

The largest negative drivers of current performance included:

- An active overweight to Consumer Staples proved challenging as the investor community continued to assess the long term impact on food and beverage demand with positive GLP-1 readouts. Packaged food holding Mondelez (MDLZ) and soft drink company PepsiCo (PEP) were particularly challenged during the period.
- Ownership of aerospace & defense companies within Industrials was a headwind to strategy performance as the group continued to face supply chain hurdles and margins remained challenged across the board. Going forward, we believe these challenges are compensated by aerospace & defense companies' fortress balance sheets and a general lack of economic cyclicality versus other Industrials sub-industries.
- An underweight to Information Technology detracted from strategy performance, although this was partially offset by strong stock selection. An underweight to systems software company Microsoft (MSFT) along with no ownership of application software companies proved challenging during the quarter. However, strong stock selection in semiconductors, and specifically the ownership of Broadcom (AVGO) and Qualcomm (QCOM), proved beneficial.

Largest Portfolio Contributors

1. **Broadcom (AVGO):** As the leader in networking integrated circuits, AVGO continued to outperform following strong product cycles and excellent customer and channel management. Additionally, ~15% of the business is currently benefiting from AI tailwinds, and the recently closed acquisition of VMware should continue to diversify revenue streams.

2. **U.S. Bancorp (USB):** As a premier regional bank, USB's fee-based business model is less asset-sensitive than peers which has typically provided stability and through-cycle performance. The 2022 acquisition of Union Bank has added material revenue, with run-rate cost synergies, and continues to provide a meaningful growth opportunity in both consumer and business banking accounts.

3. **PNC Financial Services (PNC):** During the quarter PNC posted a strong beat-and-raise following the October quarter-end and remains well positioned to continue to take market share. Conservative lending practice and high credit quality support peer-leading downside capture, as well as future earnings growth and shareholder return.

Largest Portfolio Detractors

1. **Chevron (CVX):** Earnings were pressured during the quarter compared to 2022 record levels as crude prices eased and higher costs crimped refining and chemical profits. Despite these headwinds, the outlook for CVX remains positive long-term, especially with the recent acquisition of HES which provides a foothold in Guyana's oil basins.

2. **Air Products & Chemicals (APD):** APD shares underperformed during the quarter due to inflationary cost increase announcements within the hydrogen project backlog. Long-term, APD remains well positioned to benefit from gasification market opportunities, which should drive attractive earnings and dividend growth.

3. **PepsiCo (PEP):** During the quarter, PEP shares were pressured following cautious volume guidance as a result of GLP-1 concerns and the potential trade down to private label in the case of recession. Investments in productivity and ongoing cost-reduction initiatives are expected to produce modest operating leverage in the short and intermediate term.

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Strategy Style Categorization

Asset Class	Benchmark	Mandate
Domestic Equity	S&P 500	Large Cap Core

Investment Philosophy

Bahl & Gaynor employs a Growth at a Reasonable Price discipline to purchase high-quality companies at sensible valuations. It is our goal to seek competitive performance while preserving capital in declining markets. In addition, our focus on companies that pay a growing dividend has benefited our clients in the form of a reliable income stream.

We are long-term investors and seek to identify companies that are managed conservatively and for growth, have stable and sustainable business models, and reward shareholders with a growing dividend. It is our intention to identify the best companies that meet these criteria and hold them for long periods of time.

Bahl & Gaynor's investment philosophy exemplifies our firm belief in the power of long-term investing and compounding dividend income.

Income Growth Positioning

Our Income Growth strategy focuses on generating a high level of current income that will grow over time. Protection in falling markets is a secondary goal, with long-term capital appreciation as a tertiary goal.

Bahl & Gaynor's equity selection process yields an investable universe of companies that are managed conservatively and for long-term growth, have stable and sustainable business models, and reward shareholders of the company with a growing dividend. From this investable universe, the Income Growth strategy seeks larger companies that reward shareholders with a high current dividend and have the ability to grow their dividend payments consistently in the future.

Over a full market cycle, Bahl & Gaynor's Income Growth strategy seeks to outperform its benchmark and large-capitalization core peers all in the context of a lower-than-average portfolio risk profile.

Client portfolios will generally be diversified among a selection of 40 to 50 common stock issues with each security typically held for three to five years. Low portfolio turnover combined with the favorable tax treatment of dividend income results in a cost and tax-efficient portfolio.

Portfolio Management Parameters

1. 100% of companies held in the portfolio pay a cash dividend
2. New positions must have a minimum current dividend yield of 2% at initiation
3. Portfolio typically managed to maximum 5% capital and 6% income contributions per stock
4. Cash is frictional and generally represents 1% to 3% of portfolio value
5. Annual portfolio turnover is low to moderate
6. Sell or trim decisions are based upon fundamentals, dividend policy, and better opportunities for yield or income growth
7. The strategy employs no derivatives, funds, preferred shares, MLPs, or convertible issues

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Portfolio Details

Sector	Income Growth Weight	S&P 500 Weight
Information Technology	15.8%	28.9%
Industrials	13.6%	8.8%
Health Care	13.5%	12.6%
Consumer Staples	12.6%	6.2%
Financials	11.2%	13.0%
Energy	8.7%	3.9%
Consumer Discretionary	8.4%	10.9%
Utilities	6.6%	2.3%
Real Estate	4.5%	2.5%
Materials	3.1%	2.4%
Communication Services	0.0%	8.6%
Money Market	2.0%	-

Top 10 Holdings	Income Growth Weight
Broadcom (AVGO)	5.73%
Eli Lilly (LLY)	4.09%
Merck (MRK)	4.00%
AbbVie (ABBV)	3.91%
Mondelez (MDLZ)	3.90%
PepsiCo (PEP)	3.52%
Procter & Gamble (PG)	3.30%
McDonald's (MCD)	3.20%
Air Products & Chemicals (APD)	3.13%
Chevron (CVX)	3.10%

Portfolio Statistics	Income Growth	S&P 500
P/E Ratio (trailing 12 months)	21.6x	23.0x
P/B Ratio	3.7x	4.2x
Weighted Average Market Cap	$232.1 B	$721.7 B
Dividend Yield – Gross of Fees[1]	2.8%	1.5%
A- or better S&P Quality Ranking	42.4%	26.2%
Beta since inception (Gross / Net)	0.80/0.80	1.00
Sharpe ratio	0.64/0.39	0.55

Source: FactSet, 2024. Inception date 12/31/2005.

4Q2023 Performance (Annualized)	Income Growth WRAP (Pure Gross)	Income Growth WRAP (Net)	S&P 500
1 Year	7.32%	4.16%	26.29%
3 Years	7.54%	4.37%	10.00%
5 Years	11.16%	7.89%	15.69%
10 Years	10.06%	6.82%	12.03%
15 Years	12.25%	8.94%	13.97%
Since Inception	9.76%	6.53%	9.90%

4Q2023 Risk (Annualized)	Income Growth WRAP (Pure Gross)	Income Growth WRAP (Net)	S&P 500
1 Year	12.50%	12.27%	14.11%
3 Years	15.27%	15.36%	17.29%
5 Years	16.14%	16.27%	18.37%
10 Years	13.32%	13.48%	15.13%
15 Years	13.11%	13.19%	15.33%
Since Inception	13.18%	13.26%	15.47%

Source: Bahl & Gaynor, Informa – PSN, 2024. Inception date 12/31/2005.

[1]Dividend yield includes cash holdings.
[2]Source: Bahl & Gaynor; historical downside (upside) capture is the sum of strategy returns on all S&P 500 down (up) days divided by the sum of index returns on all respective down (up) days. Down (Up) days are defined as any trading day the index posts a negative (positive) total return. Strategy performance is derived from the internal rate of return (IRR) of a single non-fee paying representative account.
[3]The income growth rate for the Bahl & Gaynor Income Growth strategy is calculated as of the most recent quarter-end using the trailing twelve months of income earned in a model portfolio, with income reinvestment, compared to the income earned in the twelve-month period one year prior. The income growth rate for the S&P 500 is proxied by the SPDR® S&P 500 ETF Trust (SPY) as an investable proxy for the Index that pays out real distributions of dividend income paid by the index constituents. SPY was chosen versus other S&P 500 Index Tracking ETFs due to its status as the largest ETF tracking the S&P 500 Index and its longer history, with an inception date of 1/22/1993, versus peers. SPY income is calculated as of the most recent quarter-end using the trailing twelve months of income earned per the distribution rate paid by the ETF, with income reinvestment at the end of each quarter, compared to the income earned in the twelve-month period one year prior.
Source: FactSet, 2024, Bahl & Gaynor. Statistics and weight data is drawn from the Income Growth model portfolio that is fully discretionary, unconstrained and subject to change. Individual Bahl & Gaynor clients may or may not hold these positions or have similar characteristics. Risk and return data are representative of the Income Growth WRAP composite. **Past performance does not guarantee future results.** Other methods may produce different results and the results for individual accounts and for different periods may vary depending on market conditions and the composition of the account. Care should be used when comparing these results to those published by other investment advisers, other investment vehicles and unmanaged indices due to possible differences in calculation methods. No alteration of the composite as presented here has occurred because of changes in personnel or other reasons at any time. Standard & Poor's (S&P) Quality Ranking: S&P determines "quality" via a company's 10-year history of earnings growth and dividend growth. Those with a quality rating of B+ (or better) are considered "average" (or better).

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Thanks

Your continued support and interest are much appreciated.

Everyone at Bahl & Gaynor would like to thank you for the opportunity to serve your investment needs.

If you would like to speak in greater detail with a member of the B&G Team, please reach out to us through our Institutional Consulting Group.

Contact Us

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