EDGEMOOR
INVESTMENT ADVISORS

Edgemoor's Quarterly Report

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Volatility Continues

The second quarter of 2022 saw a continuation of the negative momentum that began in the first quarter. Rising inflation and interest rates, as well as slowing growth in the U.S. and abroad caused sharp retreats in both the stock and bond markets.

The S&P 500 index posted a negative total return of 16.5% in the second quarter, putting it in bear market territory for the year with a negative return of 20.0%. The tech-heavy NASDAQ fared even worse, down 22.4% for the quarter and down 29.5% year-to-date. This marks the worst first half of the year for equity markets in nearly fifty years.

The bond market, as measured by the Barclay's Aggregate Bond Index, also posted negative returns, falling 4.7% in the quarter and 10.3% for the year, as rising interest rates caused bond prices to fall at a rate that exceeded their interest payments.

Inflation Soars

A major contributor to market volatility has been the sharp rise in inflation in the U.S. this year. In June, the Consumer Price Index, or CPI, the primary measure of inflation, soared 9.1%, an unexpected increase from the 8.6% rate in May. It was led by sharp increases in energy prices (up 42%) and food prices (up 10%), and is the highest level of inflation since November 1981.

This will likely prompt the Federal Reserve to continue its aggressive interest rate tightening by raising the fed funds rate another three-quarters to one percent this month, on top of the three-quarters percent increase in June, which was the largest monthly increase in short-term interest rates since 1994.

Federal Reserve Chairman Jerome Powell is standing by his recent testimony to Congress that his commitment to reducing inflation is "unconditional."

Could we be at a Peak?

Despite the numbers, it can be argued that we may be at or near a peak in inflation. Energy prices, which contributed roughly half of the June increase, have declined substantially since then, with crude oil prices dipping below $100 per barrel in July, the first time since early May.

In addition, the core inflation index, which strips out volatile food and fuel prices, slowed slightly to 5.9% in June from 6.0% in May and 6.2% in April.

If all of this is sustained, we believe it could bring down overall inflation in the coming months and reduce pressure on the Fed, allowing it to slow future rate increases.

Recession Fears

The economic debate has shifted from whether the economy will slow this year to when – and for how long – it could move into recession. A recession is generally defined as two consecutive quarters of negative GDP growth.

U.S. GDP shrank at an annual rate of 1.6% in the first quarter, the first contraction since the onset of the pandemic in early 2020. Estimates for the second quarter GDP range from negative 1% to positive 3% growth.

While we would rather not see a recession, the silver lining in a recession scenario is that an earlier recession means an earlier recovery. In other words, the sooner a recession arrives, the sooner inflation pressures will ease, and the less the Fed will have to tighten.

Consumer Spending

The biggest driver of GDP is consumer spending, which typically accounts for up to 70% of U.S. economic growth. The Commerce Department recently reported that consumer spending slowed to an annual rate of 1.8% in the first quarter, significantly weaker than the 3.1% initially reported. Consumers are cutting their spending on food, clothing, home furnishings, and appliances due to soaring prices and long supply-chain delays. In addition, the effects of pandemic-era stimulus have faded, forcing consumers to further recalibrate their spending.

Corporate Earnings

A slowdown in consumer demand can have a direct impact on corporate earnings, investment, and hiring. Although business investment has so far held up, posting 7.4% growth in the first quarter, that could reverse if companies see their ability to pass on higher input costs constrained by slowing demand and a continuing tight labor market.

Consensus estimates for 2022 corporate earnings have so far remained little changed, forecasting better than 10% earnings growth for this year, despite the fact that 70% of the companies that have issued guidance for the second quarter have trimmed their earnings estimates. We will be watching carefully how this earnings season unfolds, and would not be surprised to see a downward revision in consensus estimates for full year 2022 earnings.

Global Factors

The global economy is also facing increasing uncertainties, with the ongoing war in Ukraine and its negative impact on oil and food markets. The European Central Bank has also moved to tighten its monetary policy, albeit slightly more cautiously than the Fed.

A possible bright spot in the global economy would be the full re-opening of the Chinese economy, the second largest in the world and a major supplier of many of the goods and components that the world relies on. While Beijing has maintained its strict "zero-Covid" policy, it has reopened several manufacturing and trade hubs vital to their economy. If this continues, we believe it would be a positive factor for global economic growth.

Our Outlook

Given this backdrop, our near-term outlook is for the market to remain volatile into the second half of the year. Continuing uncertainty around inflation, interest rates, and the geopolitical risks in China and Ukraine are likely to keep investors jittery.

But longer term, our outlook remains optimistic. Pillars of strength in the U.S. economy include continuing low unemployment, positive, albeit slowing, annual GDP growth, and strong corporate and consumer balance sheets.

The June jobs report showed that U.S employers added 372,000 jobs during the month, beating expectations. And the unemployment rate remained steady at 3.6%, one of the lowest rates in decades.

We also must remind ourselves that market downturns do have an upside – that is, a resetting of asset prices can present a favorable entry point for long-term investors. The forward price-to-earnings ratio of the S&P 500 has declined to approximately 16x from a high of 23x last year, making valuations more attractive than they've been in several years.

Lower valuations mean that the long-term return potential of equities has also improved for investors. An analysis of the twelve bear markets going back to 1945 shows that the S&P 500 has returned an average of 43.7% in the twelve months after a bear market bottom. Predicting that bottom, however, is next to impossible.

Our Investment Approach

Our investment approach remains unchanged: don't panic; don't sell good investments at depressed prices; and maintain a long-term, disciplined approach to investing in high quality companies that can withstand market downturns.

We also continue to take an active approach to individual security selection and remain committed to our long-term, value-oriented investment philosophy.

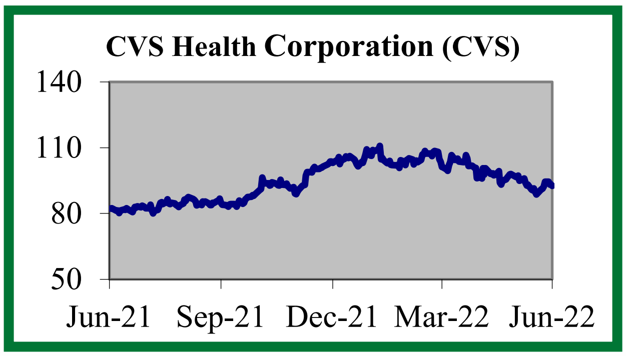
Our unique income strategy favors dividend-paying securities from a variety of asset classes, including REITs, utilities, pipeline companies, and preferred stocks. We have not been active buyers of fixed-rate bonds during the low interest rate environment of the last decade, and especially during the past two years when rising interest rates have caused bond prices to fall significantly. Instead, we favor income securities with a history of dividend growth and the potential for increasing payouts over time.

Overall, it is a challenging time for all investments, but we remain committed to selecting equity and income securities with the potential for attractive, long-term positive returns over full market cycles.

Analysis of Selected Securities

Following is a discussion of three securities we own and have bought recently. Due to factors specific to each investment, these securities are, in our opinion, priced attractively in the market today.

CVS Health Corporation (CVS)



Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 9.

Price (06/30/2022)	$ 92.66	Forward P/E	11.2
Market Cap ($B)	$ 122.9	Price/Book	1.7
Dividend Yield	2.4%	Price/Sales	0.4
Return on Equity	11.1%		

CVS Health Corporation is the nation's foremost integrated healthcare services provider. CVS has more than 9,900 retail locations, approximately 1,200 walk-in medical clinics, and more than 110 million pharmacy benefits plan members.

After acquiring insurance giant Aetna in November 2018, CVS operates in three main lines of business. The Pharmacy Services segment (approximately 45% of 1Q22 revenue) provides a full range of pharmacy benefit management solutions and processed 567 million pharmacy claims in the first quarter. The Retail/Long-Term Care segment (29%) operates retail stores and clinics and filled nearly 395 million prescriptions in the first quarter of 2022. The Health Care Benefits segment (26%) offers a broad range of health insurance products and related services.

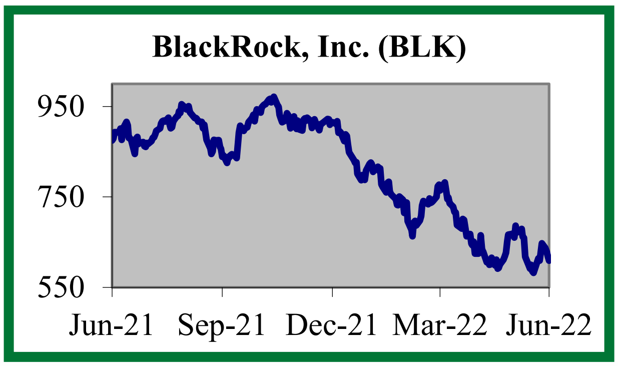
Company revenue for the first quarter of 2022 totaled $76.8 billion, which represented an 11% increase compared to the first quarter of 2021. Adjusted earnings of $2.17 per share also exceeded analyst estimates. The positive results were driven by growth across nearly all segments and prompted management to raise its full-year 2022 earnings guidance. Under new CEO Karen S. Lynch, the company has successfully integrated its retail, pharmacy, and health insurance operations which should enable CVS to accelerate earnings growth over the long term.

CVS is focused on making healthcare more accessible and affordable, as well as improving health outcomes for all its customers. About 70% of the U.S. population lives within three miles of a CVS store. This extensive reach should make it easier for an aging population to get the advice, medicines, and care they need to stay healthy and avoid more costly treatments.

The company's financial position is strong, as it generates significant cash flow that has allowed it to pay down $21 billion of debt since the close of the Aetna transaction. As a result of the reduced debt levels, the company began repurchasing stock again in 2022 and increased the quarterly dividend by 10% in February. The annual dividend has grown at a 10-year compound annual growth rate of 13%, and the shares currently yield 2.4%.

CVS shares are currently priced at 11.2 times forward earnings, which is well below the 16 times average forward P/E multiple of the S&P 500 Index. We believe CVS shares represent an attractive, long-term holding with robust growth prospects, a solid dividend, and above-average total return potential.

BlackRock, Inc. (BLK)



Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 9.

Price (06/30/2022)	$ 609.04	Forward P/E	15.9
Market Cap ($B)	$ 91.4	Price/Book	2.5
Dividend Yield	3.1%	Price/Sales	4.8
Return on Equity	16.9%		

BlackRock is the largest asset manager in the world with $9.6 trillion in total assets under management (AUM) as of March 31, 2022. BlackRock provides investment management, risk management, portfolio construction, and advisory services to institutional and retail clients in over 100 countries across the globe. Its range of offerings includes both actively and passively managed investment products, separately managed accounts, and other pooled investment vehicles. In the highly competitive asset management industry, BlackRock's greatest competitive advantages are its size and scale, its leading market share in both passive and active strategies, its focus on institutional investors, and its solid long-term performance and reasonable fees.

Over the past two decades, BlackRock has benefited from the rise in popularity of passive investment products, which are designed to track a benchmark index and offer lower costs. Passive products account for roughly two thirds of BlackRock's long-term AUM and nearly half of its revenues. BlackRock's iShares platform is the largest domestic and global provider of exchange traded funds, with an estimated 34% global market share that is well ahead of second-place Vanguard.

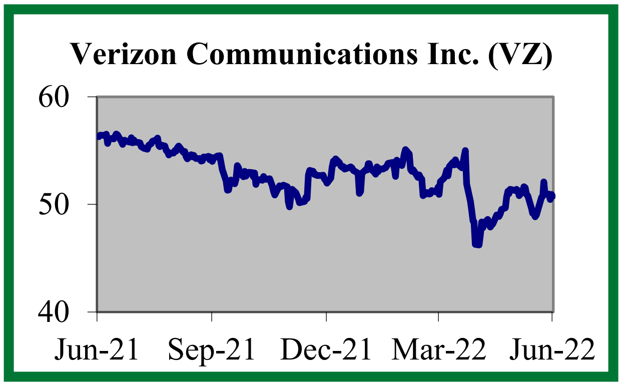
Institutional clients account for approximately 80% of BlackRock's total AUM. These investors tend to be more stable and trade in and out of funds less frequently than individual retail investors, which has allowed BlackRock to generate higher and more stable revenues and growth rates than many of its peers.

BlackRock is financially strong and shareholder friendly. Its balance sheet has minimal debt which carries an AA- credit rating from Standard and Poor's. The stock pays a growing and sustainable dividend that currently yields 3.1%.

The recent market sell-off, ignited by higher interest rates and the Russia-Ukraine war, has been a drag on the near-term outlook for BlackRock. However, once markets recover, we believe BlackRock is well positioned to resume long-term growth due to its demonstrated ability to acquire and retain a high proportion of client assets through investment cycles.

We consider BlackRock shares to be attractively valued at 15.9 times forward earnings, well below the five-year historical average of 18.3 times.

Verizon Communications Inc. (VZ)



Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 9.

Price (06/30/2022)	$ 50.75	Forward P/E	9.5
Market Cap ($B)	$ 213.1	Price/Book	2.5
Dividend Yield	5.0%	Price/Sales	1.6
Return on Equity	27.6%		

Verizon Communications is one of the world's leading providers of communications, technology, information, and entertainment products and services to consumers, businesses, and government entities. The company has two reportable segments: Verizon Consumer Group and Verizon Business Group. The Consumer segment provides consumer-focused wireless and wireline communications services and products. The Business segment provides wireless and wireline communications services and products, including data, video and conferencing services, corporate networking solutions, security and managed network services, local and long-distance voice services, and network access to deliver various Internet of Things (IoT) services and products.

Verizon is primarily focused on the wireless business, where it believes its networks provide multiple avenues for growth. The firm has taken steps to ensure it remains well positioned in the traditional wireless business, building fiber deeper into major metro areas, acquiring a large amount of telecom spectrum in 2021, and ramping up spending to put that spectrum to use. In the wireless business, which generates about 70% of total revenue and accounts for nearly all of Verizon's profits, the company holds approximately 40% of the U.S. postpaid phone market. Together with AT&T and T-Mobile, the three companies control most of the U.S. wireless market, claiming more than a combined 90% of the retail postpaid phone market.

Verizon has long prided itself on its network, continually investing in technology to ensure that it delivers the highest network quality to its customers. Verizon was the first company in the world to launch commercial 5G, the fifth-generation mobile wireless technology that offers massive data capacity delivered at ultra-fast speeds, for mobility, fixed wireless, and mobile edge computing. As of December 31, 2021, Verizon's 5G Ultra-Wideband is available in parts of 87 U.S. cities.

Investing consistently in both wireless and fixed-line technology, the firm has built its brand reputation around these networks, attracting a large and loyal customer base. Leading scale enables Verizon to generate the highest margins and returns on capital in the industry, despite heavy investment.

We consider Verizon a core, long-term income holding, as the stock offers an attractive and growing dividend, currently yielding 5.0%, and is reasonably valued at 9.5 times forward earnings, meaningfully below the five-year historical average of 11.4 times.

Source for text and charts: Morningstar, S&P/CFRA, Schwab, ValueLine, Black Diamond Performance Reporting, Yahoo Finance, Bank of America, and Argus reports.

Edgemoor Investment Advisors is an independent wealth management firm providing investment and financial planning advice to individuals, retirement plans, trusts, family foundations, and an equity mutual fund. We manage approximately $964 million as of June 30, 2022, for our clients and focus on long-term capital appreciation, preservation of capital, and income generation through disciplined management of value-oriented equity and income portfolios. Please contact us if you would like more information.

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The S&P 500 index is an unmanaged market-capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation to represent U.S. equity performance. The S&P 500 index is discussed for comparative purposes only. The comparisons have limitations because the indexes have volatility, investment, and other characteristics that differ from the investment strategies of Edgemoor. Further, it is not possible to invest directly in the indexes.

The Barclays U.S. Aggregate Bond Index is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States. The Index is frequently used as a stand-in for measuring the performance of the U.S. bond market. In addition to investment grade corporate debt, the Index tracks government debt, mortgage-backed securities (MBS) and asset-backed securities (ABS) to simulate the universe of investable bonds that meet certain criteria. In order to be included in the Index, bonds must be of investment grade or higher, have an outstanding par value of at least $100 million and have at least one year until maturity.

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