EDGEMOOR
INVESTMENT ADVISORS

Edgemoor's Quarterly Report

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Different Worlds

It is remarkable how much our world has changed from the one we knew in February. Since then, we have significantly altered our daily lives, schools have shifted to remote learning, millions of workers have adjusted to working from home or lost their jobs, and the stock market and economy have seesawed. The COVID-19 pandemic has caused human pain, suffering, and loss, and it may be a long time before our world returns to its previous state.

We are now living with the great uncertainties of the COVID-19 pandemic, the economy, and the hotly contested elections for the presidency and Congress. Following are our views on what has been happening and where we think we are heading. We remain confident that our nation and world will get through this difficult period, but we expect more market volatility while we await an eventual return to normalcy.

Third Quarter in Review

Following the sharp downturn in the stock market in February and March and the similarly fast rebound in the second quarter, stocks continued to rise steadily through July and August, hit a new record high on September 2nd, and then fell back almost 10% before recovering. For the third quarter, the S&P 500 index returned 8.9% including dividends and ended September up 5.6% for the year.

Reports during the third quarter confirmed the dramatic economic impact of the surge in COVID-19 cases in the United States and abroad and the resulting restrictions on activity. Second quarter GDP declined 31.4% after dropping 5% in the first quarter, and corporate earnings fell 32% in the second quarter.

On the jobs front, businesses hired fewer workers than in the second quarter and slowed the pace of hiring each month. Nevertheless, this hiring caused the unemployment rate to drop to 7.9%, after peaking at nearly 15% in April. Even after the recent additions, however, more workers have lost their jobs than in the 2008-2009 financial crisis, and only about half of the 22.2 million people laid off or furloughed in the early days of the pandemic have returned to work.

The U.S. Federal Reserve remained steadfast in its commitment to supporting the economy and revised its policy to allow inflation to rise for longer before triggering a Fed move to increase interest rates. Meanwhile, disagreement over the size and details of another stimulus measure has prevented Congress and the White House from offering additional relief that we were hoping to see.

Observations and Outlook

We have been both impressed and a bit surprised by the stock market's resilience. While we did expect stocks to recover from their initial drop, the rally continued steadily for months despite worrisome signs during the third quarter related to the ongoing pandemic and economic recession.

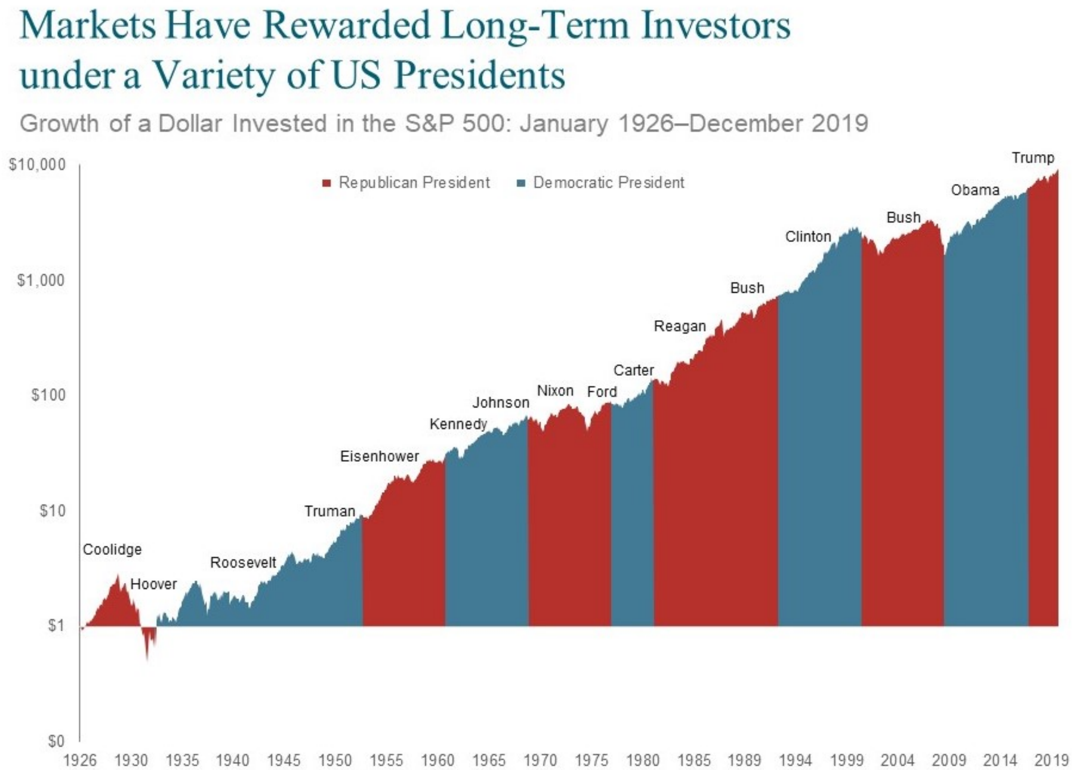
Technology companies and others involved in the digital economy have generally prospered despite the pandemic, partly due to the demand for their services from employees working and households provisioning remotely. Businesses maintaining high levels of activity and profitability include those providing necessities and home products, such as grocery stores, online retailers like Amazon, big discount stores, and large home improvement retailers Lowe's and Home Depot. These businesses have largely maintained or even increased their workforces, providing job security that supports consumer spending and economic growth. Homeowners have benefited from rising home prices, and employees with bachelors' degrees or higher have mostly returned to work, much of it remote.

Other sectors and less educated workers have not fared as well. Travel and entertainment companies have experienced dramatic reductions in revenues and have resorted to layoffs. Restaurants have also struggled as increased takeout and delivery orders and outside dining have not fully offset the losses of indoor dining capacity and increased costs incurred to operate safely. We are concerned that many of the most vulnerable workers, including those who have lost their jobs in these industries, will be forced to cut spending now that the extra unemployment benefit has expired. More temporary furloughs have become permanent, and we believe many unemployed workers will likely remain unemployed over a long time.

So far, the stronger recovery in certain sectors, the associated rebound in white collar jobs, and the return of the stock market to near record levels have combined with monetary support from the Fed and fiscal help from Congress to enable many parts of the economy to improve from the depths of March and April. Economists expect GDP to rise in the third quarter compared to the second at an annual rate of around 24%. However, we believe unemployed workers will need substantial additional help from Congress and the White House, and we are disappointed by the lack of support so far. Without further action, a decrease in consumer spending across a broad swath of the population will likely leave the United States mired in an economic downturn.

Reflecting the decline in economic activity, corporate earnings are likely to be 21% lower in the third quarter and 12% lower in the fourth compared to last year. However, analysts currently expect a 26% uptick in 2021 as the economy regains its footing and comparisons are to 2020's depressed levels. We are focusing on prospects for 2021 and beyond as we evaluate investment opportunities.

The upcoming elections will be the primary focal point for the next several weeks, and the heated rhetoric and strong emotions portend more volatility in the markets until we get a clear resolution of the outcome. Despite what many people believe, the stock market has performed well during presidential terms no matter which party occupies the White House, as shown in the chart below.



Past performance is not a guarantee of future results. Indices are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. Source: S&P data © 2020 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

Conclusion of the elections will remove much of the uncertainty now hanging over the markets as we await the results. Greater clarity on policy approaches for a comprehensive effort to control and, eventually, vaccinate against COVID-19 and to reopen the economy would enable us to return to normalcy. We are also dependent upon similar efforts around the world, given the importance of international trade and the need to prevent further spread of the pandemic.

We have confidence in our nation and our markets, and we know we will emerge from the current situation and resume economic growth. In the meantime, we are largely sticking with our long-term investment strategy, and we are investing some cash to take advantage of current opportunities. Even now, we are still able to find both stock and income investments that we believe will provide attractive long-term returns to patient investors.

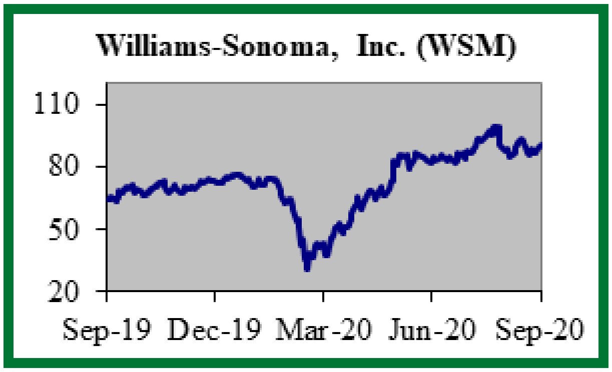
Remote Office Operations

We continue to work remotely, have been able to fully carry on our work, and are readily available by phone or email. We will work remotely until being together is clearly safe for all of us. If you need to send anything to us by mail, FedEx, or UPS, please contact Anne at 301-543-8881 or abaker@edgemoorinv.com for instructions. Stay safe and healthy.

Analysis of Selected Securities

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

Williams-Sonoma, Inc. (WSM)



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

Price (09/30/2020)	$ 90.44	Forward P/E	15.8
Market Cap ($B)	$ 7.4	Price/Book	5.5
Dividend Yield	2.1%	Price/Sales	1.2
Return on Equity	33.5%		

Williams-Sonoma is a specialty retailer of home furnishings and decor. The San Francisco-based company operates 616 retail stores under the Williams-Sonoma, Pottery Barn, Pottery Barn Kids, PBTeen, and West Elm brands, with most locations in the United States. Retail sales accounted for 44% of total fiscal year 2020 revenues of $5.9 billion, while the fast-growing e-commerce and direct-mail business accounted for 56% of total revenues.

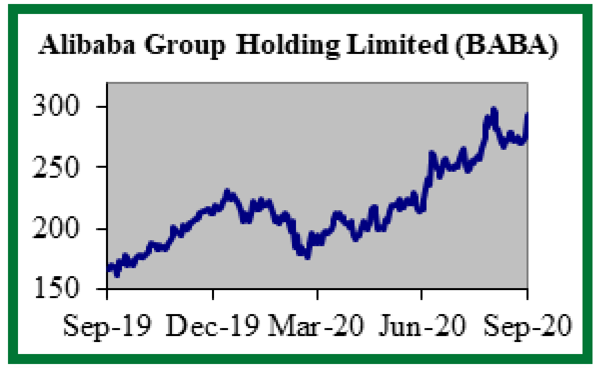
Williams-Sonoma has carved out a solid niche in the highly fragmented $116 billion home furnishings industry by successfully combining its expertise in digital marketing and e-commerce analytics with a track record for developing unique and proprietary products sourced on an exclusive basis from vendors around the world. The company's data-driven business model has allowed Williams-Sonoma to capture significant market share, drive strong customer loyalty, and generate market-leading profitability.

With over half of its sales derived from its e-commerce strategy, Williams-Sonoma has been able to build its brands efficiently and cost-effectively among customers who increasingly shop online. The acceleration of online purchasing during the COVID-19 pandemic has benefited Williams-Sonoma significantly, as the company saw e-commerce sales increase 40% in the second quarter of 2020. The shift of wallet share from travel and entertainment to in-home investments is expected to continue even as stay-at-home orders are lifted and should drive continued growth and profitability for Williams-Sonoma brands for years to come.

The company's sophisticated data analytics come from having collected data and buying patterns on its customers for more than 25 years, and the resulting deep customer knowledge has allowed Williams-Sonoma to build new brands based on both predictive and demographic patterns of buying. For example, the West Elm brand, launched in 2002 and the company's highest growth segment, caters to the lifestyle cycles of millennials, targeting their initial home furnishing purchases. As they age and upgrade, these customers become natural consumers of higher-ticket products from Pottery Barn and Williams-Sonoma. And as they marry and have children, they in turn become natural buyers of PB Kids and PB Teen products. This attention to the full life cycle of its customers means less capital is needed to generate the next incremental sale and has led to loyal customers, sustainable and growing brands, and industry-leading profit margins.

Williams-Sonoma is financially sound and shareholder friendly. Its return on equity tops 33%, and its five-year return on invested capital is better than 19%, both higher than peer and industry averages. The company has consistently grown its dividend, and the shares currently yield 2.1%. Its balance sheet is sound, with $950 million of cash and $2.1 billion of debt as of June 30, 2020. Williams-Sonoma shares are attractively valued at 15.8 times forward earnings, compared to a market average of about 22 times for the S&P 500 index.

Alibaba Group Holding Limited (BABA)



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

Price (09/30/2020)	$ 293.98	Forward P/E	31.1
Market Cap ($B)	$ 783	Price/Book	6.6
Dividend Yield	0%	Price/Sales	9.8
Return on Equity	23.9%		

Alibaba Group is among the world's largest online and mobile e-commerce companies, providing technology, marketing, and logistics services to help businesses in China and worldwide establish an online presence and sell their products and services. Alibaba's ecosystem includes several of China's most-frequented online retail platforms: Taobao Marketplace (China's largest online consumer-to-consumer shopping site), Tmall (China's third-largest business-to-consumer website), and Juhuasuan (China's most popular group buying marketplace). Together, these three sites generated $1 billion of gross merchandise value in fiscal year 2020, more than Amazon's and eBay's combined China sales. The Alibaba sites also had more than 740 million active annual users and 875 million active mobile users, representing an 83% penetration rate of all Chinese internet shoppers.

In addition to this Core Commerce business, which generates approximately 85% of total company revenues, Alibaba also operates in three other business segments: Cloud Computing (9% of total revenues), Digital Media and Entertainment (5%), and Innovation Initiatives (1%). The company's cloud computing business, AliCloud, has experienced a sharp acceleration in demand due to the global pandemic, with revenues rising 57% in the latest quarter. AliCloud should become a major revenue and cashflow contributor as companies and government groups increasingly move to outsource information technology and reduce expenditures.

Alibaba's interconnected businesses create a strong network effect for the company, as the value of the platform to consumers increases with the greater number of sellers, and vice versa. In addition, these interconnected businesses provide the company with an unparalleled source of data that it can cross-sell to merchants to help them develop personalized marketing and brand strategies. The power of this network effect is the primary source of Alibaba's wide economic moat, the protection from competition that we seek in investments.

Financially, Alibaba is exceptionally strong, with $385 billion of cash and $125 billion of long-term debt as of June 30, 2020. The company generates $550 billion of annual revenues and $150 billion of free cash flow and enjoys 45% gross profit margins and 24% average return on equity. Overall, we think Alibaba is well positioned for continued growth in China and elsewhere, given the breadth and depth of its product offerings, its multitude of services for cross-border commerce, and its valuable first mover and brand awareness advantages.

The Blackstone Group Inc. (BX)

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

Price (09/30/2020)	$52.20	Forward P/E	19.6
Market Cap ($B)	$ 37.3	Price/Book	6.5
Dividend Yield	3.5%	Price/Sales	12.1
Return on Equity	19.6%		

The Blackstone Group is one of the world's largest managers of alternative assets, including private equity, real estate, hedge funds, credit funds, and closed-end mutual funds. Its total assets under management (AUM) topped $564 billion as of June 30, 2020, and management's goal is to nearly double AUM to $1 trillion by 2028.

Blackstone converted from a limited partnership to a corporation in July 2019, greatly expanding the market for its shares. The company estimates that 60% of U.S. equity index funds and exchange-traded funds, representing $7.5 billion of assets, are restricted from owning partnerships, so the conversion to a corporation has enabled the stock to be included in a wider range of stock funds.

Blackstone's significant AUM growth in recent years has also been accompanied by a sharp rise in fee-related earnings, up 12% in the most recent quarter to $436 billion. The company is targeting

75% growth in fee-related earnings over the next several years to 65% of total earnings, up from 45% currently. Higher fee-related income reduces the variability of earnings, raises the prospect for higher dividend distributions to shareholders, and potentially increases the valuation multiple applied to shares.

Although the COVID-19 pandemic may impact asset sales and valuations in the near term, Blackstone is well positioned to take advantage of new investment opportunities at attractive valuations with $155 billion of committed but uninvested capital. A particular area of interest is infrastructure, and Blackstone recently raised $14 billion in its inaugural infrastructure fund to target investments in transportation, energy, communications, and water and waste management projects in the United States and worldwide.

Blackstone pays a substantial and growing dividend, and the shares currently yield 3.5%. As a best-in-class asset manager with a long track record of successful investing and numerous avenues for growth, Blackstone represents an attractive long-term investment with significant income-generating appeal.

Source for text: Morningstar, S&P, Schwab, ValueLine, Argus, Credit Suisse, Black Diamond Performance Reporting, and Yahoo Finance.

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 $1.04 billion as of September 30, 2020 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 MSCI ACWI ex USA Investable Market Index (IMI) is an unmanaged market-capitalized-weighted index of 6,472 large, mid, and small cap stocks from 22 developed and 24 emerging markets outside the United States. The index covers approximately 99% of equities outside the United States. The Bloomberg Barclays U.S. Aggregate Bond index is a broad-based, market-value-weighted index that measures the performance of the U.S. dollar denominated, investment-grade, fixed-rate, taxable bond market. Sectors in the index include Treasurys, government-related and corporate securities, mortgage-backed securities (MBS), agency fixed rate and hybrid ARM pass-through asset-backed securities (ABS), and commercial mortgage-backed securities (CMBS). The S&P 500 index, MSCI ACWI Ex USA IMI index, and Bloomberg Barclays U.S. Aggregate Bond index are 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.

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