EDGEMOOR
INVESTMENT ADVISORS

Edgemoor's Quarterly Report

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The Great Re-Emergence

The U.S. economy and financial markets accelerated their recovery in the second quarter of 2021 from the Covid-19 pandemic that kept Americans and the world in its grip for more than 15 months. Several factors have contributed to the robust recovery.

First, increasing vaccination rates in most parts of the U.S. have led to the easing of pandemic-related restrictions, which in turn have boosted economic activity and consumer spending. It is estimated that the U.S. consumer accumulated more than $2.1 trillion in incremental savings during the pandemic and is now spending those savings on pent-up demand for travel, entertainment, and dining out.

Second, the Federal Reserve has remained committed to low interest rates and accommodative monetary policies, spurring everything from home purchases to corporate investment. Finally, government stimulus appears to be continuing with a bipartisan infrastructure spending program likely to pass in Congress and succeed months of federal Covid-19 relief spending.

The pace of the economic recovery has been faster and stronger than expected, with the Fed revising its estimates for 2021 GDP growth upward from 4.2% in December to 6.4% in March and to 7% by mid-June. Some economists are even more bullish, predicting that GDP could grow at an annualized rate of 8% - 9% this year.

Mid-Year Review

The strong uptick in economic activity has led to a robust rebound in corporate earnings, which increased 143% in the first quarter of 2021 from the pandemic low-point of the first quarter of 2020, and are expected to top 65% year-over-year growth in the second quarter. For the full year 2021, S&P 500 earnings estimates, which have continued to be revised upwards by most analysts, are projected to grow 53% year-over-year to $187 per share, followed by another 12% growth in 2022 to $210 per share, reflecting the strong and sustained growth expected for the U.S economy over the next two years.

All of these factors have fueled stock market gains of 15.3% for the S&P 500 year-to-date through June 30th, with most stock indices reaching record highs at the end of the quarter.

The employment picture has also brightened in 2021. After a blockbuster employment report in March, job growth slowed in April but recovered in May and June, sending the unemployment rate down to 5.9%. However, in a frustrating twist to employers, job postings are at record levels even as nine million Americans remain unemployed, meaning many businesses can't fill the positions they need to return to full capacity. With most supplemental unemployment benefits expiring by

September, these distortions in the labor market are expected to ease by the fourth quarter of 2021.

Looking Ahead

As the U.S. economy comes back from the depths of the pandemic, many investors now see inflation as the next serious risk to the economy and markets. Stoking this fear, consumer prices rose at an annualized rate of 5.4% in June, marking a 13-year high and raising concerns that inflation may rise further and be more sustained than the Federal Reserve currently expects. However, in its latest Federal Open Market Committee meeting, the Fed remarked that the current burst of inflation, seen especially in rising commodity, energy, and other raw material prices, is likely to be transitory. The Fed sees inflation peaking in the second quarter at 3% before dropping back to 2% by the end of 2021, as global supply chains recover and the supply/demand relationship for most goods and services comes more into balance.

Fears of inflation have also put the spotlight on interest rates; specifically, how and when the Fed might respond by raising rates and curtailing asset purchases. The Fed has a number of tools in its arsenal to prevent excessive inflation. First, it could address short-term interest rates by raising the fed funds rate, which impacts the cost of credit card debt and bank loans for consumers and businesses. Raising those debt costs inherently reduces spending, which taps the brakes on rising prices.

The Fed could also begin tapering its Quantitative Easing (QE) program, under which it has been buying $120 billion of U.S. Treasury bonds and mortgage-backed securities each month since June 2020. The effect of QE is to increase the money supply while driving down long-term interest rates. By gradually reducing its asset purchases, the Fed would reduce the money supply and push long-term rates higher, which, together with increasing short-term rates, could cause a gradual decline in consumer and housing prices as debt costs rise.

Given its view that current inflationary pressures are transitory, the Fed has not indicated any material change to its monetary policy, meaning that it does not expect any rate hikes to be needed until 2023.

World Markets

The sustainability of the U.S. recovery will depend in part on the pace and strength of the recovery elsewhere in the world. After re-entering recession in early 2021 and stumbling through the initial phase of its vaccination campaign, the outlook in Europe has improved and appears to be gaining momentum. Retail establishments in all 27 European Union countries have now reopened and governments are easing restrictions and allowing more economic activity, especially in the service sector. As a result, European growth is now projected to reach 4.2% in 2021.

The economic outlook for the developing world, many parts of which have limited access to vaccines and are still battling surging Covid-19 numbers, is mixed but still positive overall.

Outlook

We remain optimistic that the U.S. economy and financial markets will continue their positive trajectory through 2021 and into 2022 as businesses and consumers continue to recover from the Coronavirus pandemic. Overall, the combination of pent-up consumer demand, supportive monetary and fiscal policies, improving business and consumer confidence, and reopening momentum provide a favorable backdrop for continued growth in the U.S. economy and financial markets.

Having said this, we would not be surprised to see increased market volatility, as investors remain skittish about buoyant asset values and continue to parse every word out of the Fed's FOMC meetings.

Edgemoor Portfolio Implications and Actions

We do not anticipate major changes to our portfolios as a result of current trends. We continue to hold and to look for attractively priced investments that might benefit from infrastructure spending and the broader economic recovery, which have the potential to boost value stocks, in particular. Rising interest rates do not concern us now, but we will be keeping a close eye on yields and signs of an uptick in inflation.

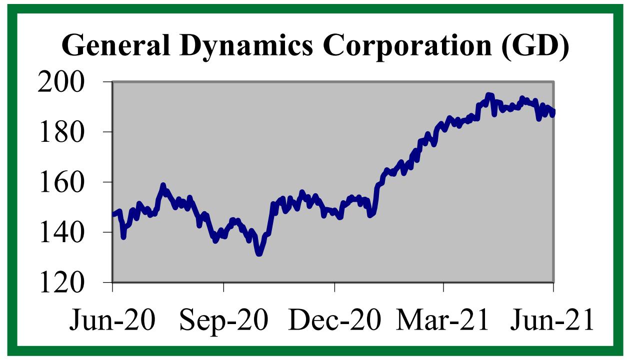
Edgemoor Office Re-Opens

We are pleased to announce that Edgemoor's office has fully re-opened as of June 1st, 2021. We successfully worked from home during the pandemic and are now enjoying being back in the office. We welcome all clients who would like to return to in-person meetings to give us a call and set up an appointment.

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.

General Dynamics Corporation



Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 8.

Price (06/30/2021)	$ 188.26	Forward P/E	17.0
Market Cap ($B)	$ 53.5	Price/Book	3.5
Dividend Yield	2.5%	Price/Sales	1.4
Return on Equity	22.2%	Debt/Equity	0.7

Virginia-based General Dynamics is the world's fourth largest defense contractor and the second largest manufacturer of corporate jets. The company operates in four primary business lines: Aerospace (21% of 2020 revenues), Combat Systems (19%), Marine Systems (26%), and Technologies (34%). The company derives approximately 69% of its revenues from the U.S. government, 9% from foreign governments, and the remaining 22% from commercial customers. General Dynamics's well-diversified business mix and entrenched product offerings are the source of the company's leading market positions and wide economic moat. The company ended the first quarter of 2021 with a record backlog of $89.6 billion, equivalent to more than two years of revenue, which provides a high degree of visibility into future years' sales.

The Aerospace segment, which is predominantly composed of Gulfstream jets, enjoys a commanding position in the high end of the large-cabin business jet market. This segment provides diversification from defense spending, which is a unique advantage General Dynamics has over many of its peers in the defense contractor industry. While business jet utilization and new orders were strained during the Covid-19 pandemic, sales activity has begun to recover, and management believes this trend will strengthen in the second half of 2021. In addition, the highly anticipated introduction of Gulfstream's G700 at the end of 2022 should be an important driver for the company's business jet sales for years to come.

General Dynamics's Combat Systems segment produces land-based vehicles, such as the Abrams tank, which has been the main battle tank of the U.S. Army since entering service in the 1980s. General Dynamics should continue to benefit from the incumbency advantage over its competitors in this large and stable market.

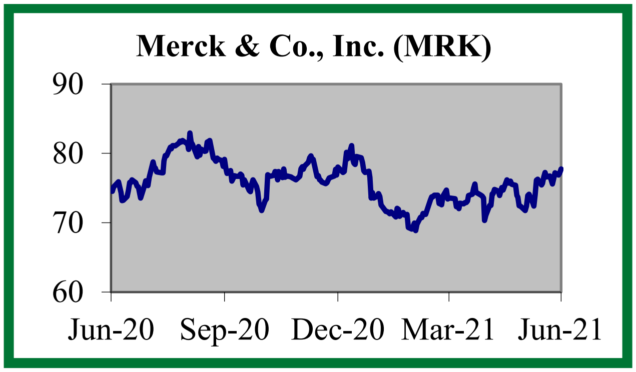
The company's Marine Systems segment, which operates as one of only two major shipbuilders in the U.S., enjoys one of the widest economic moats in the defense industry. The segment accounts for nearly 56% of the company's $89.6 billion backlog, providing consistent and highly visible earnings over multi-decade procurement cycles. The crown jewel of the Marine Systems segment is a $9.5 billion contract for the development and construction of the first two Columbia-class nuclear submarines, scheduled to be delivered in 2028 and 2031.

The Technologies segment includes IT Services and Mission Systems, the latter of which provides mission-critical products for military applications. Mission Systems is a durable and profitable business for General Dynamics due to its large installed base of products and high customer switching costs.

General Dynamics has committed itself to shareholder friendly policies, highlighted by 24 consecutive years of dividend increases and the use of excess cash to buy back its stock. Over the past five years, General Dynamics has returned nearly $12 billion to shareholders in the form of dividends and share repurchases.

We believe General Dynamic stock is attractively valued at 17 times 2021 earnings per share, given the company's steady growth and high visibility of future earnings.

Merck & Co., Inc.



Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 8.

Price (06/30/2021)	$ 77.77	Forward P/E	12.4
Market Cap ($B)	$ 197.8	Price/Book	7.4
Dividend Yield	3.3%	Price/Sales	4.2
Return on Equity	26.4%		

Merck is a global healthcare company that delivers innovative health solutions through its prescription medicines, vaccines, biologic therapies, and animal health products. The company's operations are principally managed on a products basis and include two operating segments: Pharmaceuticals (88% of sales) and Animal Health (12%). Merck has a strong global presence, as 43% of sales were earned in the United States and 57% internationally.

The Pharmaceutical segment includes prescription drugs and vaccine products focused on the treatment of cancers, diabetes, HIV, and other chronic conditions. Merck's top-selling products include blockbuster drugs Keytruda (cancer, 30% of sales), Januvia (Type-2 diabetes, 11%), and Gardasil (HPV vaccine, 8%). Keytruda, with over $14 billion in 2020 sales, enjoys a fist-mover advantage in the treatment of non-small cell lung cancer, and has also received FDA approval for several new oncology applications. Keytruda does not face loss of patent exclusivity until 2029 and so should enjoy continued growth in sales and profit margins for several years to come.

The Animal Health segment develops, manufactures, and markets a wide range of veterinary pharmaceutical and vaccine products, as well as health management solutions and services for the prevention, treatment, and control of disease in all major livestock and companion animal species. Merck also offers an extensive suite of digitally connected identification, traceability, and monitoring products. The company sells its products to veterinarians, distributors, and animal producers.

On June 3, 2021, Merck completed the spinoff of Organon & Co., which included the company's women's health products, mature brands, and biosimilars. Following the spinoff of Organon, Merck's remaining portfolio holds a higher percentage of drugs with strong patent protection, which should result in stronger growth and higher profit margins. Specifically, the divestment will allow Merck to focus on the development of new oncology drugs, vaccines, and hospital and specialty products.

Merck has demonstrated a commitment to shareholder friendly policies, paying a dividend for nearly fifty years and increasing it each year since 2011. The company has further enhanced shareholder value by using excess cash to buy back its stock. Over the past five years, Merck has returned $50 billion to shareholders in the form of dividends and share repurchases.

Merck shares are currently trading at 12.4 times 2021 consensus earnings estimates, meaningfully below its five-year average multiple of 14.9. In addition, the stock pays an attractive and growing dividend, currently yielding 3.3%. As such, we believe Merck shares are an attractive core holding for investors.

Blackstone Mortgage Trust, Inc.

Source for chart and financials: Yahoo Finance and Morningstar. Past performance is not indicative of future results. Please see disclosures on page 8.

Price (06/30/2021)	$ 31.89	Forward P/E	13.1
Market Cap ($B)	$ 4.7	Price/Book	1.2
Dividend Yield	7.9%	Price/Sales	10.3
Return on Equity	7.2%		

Blackstone Mortgage, one of our income holdings, is a real estate investment trust that originates senior loans collateralized by commercial real estate in North America, Europe, and Australia. Backed by the Blackstone Group, the largest alternative asset manager and a major real estate investor with a $368 billion global real estate portfolio, Blackstone Mortgage enjoys proprietary access to market information, deal flow, and some of the top institutional real estate investors in the world.

Newly appointed CEO Katie Keenan brings significant experience and expertise to the role. In addition to her position at Blackstone Mortgage, she also serves as a Senior Managing Director in the Blackstone Real Estate Debt Strategies group, and as a member of the Real Estate Investment Committee for both Blackstone Real Estate Debt Strategies and Blackstone Real Estate Advisors.

Blackstone Mortgage's portfolio consists of 122 loans spread across a variety of property types including office (54%), hospitality (17%), multi-family (12%), and industrial (4%). The portfolio is also geographically diversified, holding investments in major markets like New York (20%), California (14%), and numerous locations across Europe (29%). Loans are secured by high-quality, institutional assets sponsored by some of the best-capitalized real estate owners and operators in the world.

Blackstone Mortgage closed $1.7 billion of new loans in the first quarter of 2021, surpassing its originations for all of 2020. The total loan portfolio also reached a record $18.7 billion at quarter-end, while continuing to enjoy strong credit metrics with 98% of loans performing and 100% interest collected.

The commercial real estate market will likely benefit from a recovering economy and the easing of COVID-induced restrictions as vaccination rates rise. Blackstone Mortgage's robust liquidity positions it well for future investment opportunities and its largely floating rate loan portfolio means earnings would grow if interest rates continue to rise. The company's fundamentals are also attractive, with the shares currently trading at a forward price/earnings ratio of 13.1 and paying an above-market yield of 7.9%.

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 $1.3 billion as of June 30, 2021 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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