EDGEMOOR INVESTMENT ADVISORS

Edgemoor's Quarterly Report

Suite 315
7250 Woodmont Avenue
Bethesda, MD 20814
301-543-8881
www.edgemoorinv.com
www.edgemoorblog.com

April 2016

The thing about a roller coaster is that you get off at the same place as you got on, but you might feel queasy after the ride. *Barron's* 4/2/16

Moving Right Along

After the roller coaster ride in stocks during the first quarter, investors are happy to be moving into spring with hopes of calmer markets. Oil prices, corporate earnings, central banks' plans, and global economic prospects are all competing with the U.S. Presidential primaries for the most headlines. We expect more volatility ahead but also see reasons to expect modest gains for stocks, and we think most of the good economic and earnings news will come in the second half of the year.

What a Start to 2016

Stocks plunged from the outset this year, mostly due to continued declines in oil prices, expectations of more rate increases from the U.S. Federal Reserve, and slowing growth in China. The S&P 500 index entered official correction territory (down more than 10% from its May 2015 peak) in February before rebounding to end the quarter about where it began. After several years of relative calm, U.S. stock volatility spiked in August of last year and again at the beginning of 2016. Stocks dropped during the quarter in Europe, China, and Japan, continuing a streak of U.S. outperformance.

The immediate catalyst for market angst came in early January from China, where the government's attempts to stabilize markets spooked investors and heightened concern about global economic growth, mirroring the government's action and the market's reaction in August of last year. In addition, oil prices continued their plunge in January as demand remained low and supplies high, while inventories rose. Adding to worries was the fear of many investors that the Fed's plans for additional rate hikes in 2016 might derail the U.S. recovery.

In mid-February, oil prices began to rally from their lows as key nations discussed a potential production freeze, the Fed emphasized its determination to focus on economic data and avoid raising rates too quickly, and conditions in China settled somewhat. Investors decided the markets had overreacted to the various concerns and began seizing the opportunity to buy at reduced prices, which led to a steady rise in the S&P 500 index through the end of March.

Outlook – All About Earnings

We are encouraged by the recent signs of more stability in the stock market, as well as general strength in the U.S. economy, though economic growth in the rest world is likely to be more elusive in 2016. Overall, we are optimistic about corporate earnings, despite expectations for disappointing first quarter results. We anticipate that earnings, which are the foundation of stock valuations, will be better in the second half of the year than in the first and combine with reasonable valuations to result in modest gains through year-end.

We think the U.S. economy will remain on its path of slow, steady expansion, with GDP rising about 2% for the full year. The most recent employment report indicated robust March jobs growth of 215,000, an increase in the labor force participation rate, and a slight rise in wages, all of which should support higher consumer spending. The latest manufacturing sector data reflected expansion for the first time since August 2015, the service sector has now been growing for over six years, and the housing market is strong. Based on these positive trends, we believe it is unlikely that the U.S. economy will enter a recession anytime soon.

Elsewhere in the world, the economic picture is mixed. European economies generally show slow growth at rates lower than in the United States. Japan is struggling to avoid falling into a recession, largely due to weakness in certain of its export markets that is now exacerbated by the strengthening yen, but we are optimistic that the increased focus on profitability and shareholder returns under Prime Minister Abe's policies will help to improve the country's economy. China's GDP is still expanding at about 6% annually, a rate far above that of most of the developed world but lower than China's historical rate. This slowing growth has contributed to the decline in commodity prices and hurt many developing nations that depend on the Chinese market for sales of their natural resources.

The U.S. Federal Reserve and other central banks are closely monitoring conditions and pursuing policies to boost investment, lending, and spending. Based on recent comments from the Fed reflecting some concerns about the domestic and global economies, we now expect only one or two Fed rate hikes through the end of 2016. The European Central Bank is broadening its stimulus measures to include purchases of non-financial corporate bonds, and the Bank of Japan has pushed interest rates to negative levels in an attempt to fight deflation and encourage spending and investment. As the Chinese government strives to manage its currency valuation and promote consumption, we think conditions there will remain volatile.

The imbalance between supply and demand for oil and other commodities will likely linger, keeping prices low until global demand picks up, supplies tighten, or both. Oil has rebounded from a low of $26 per barrel to about $40 currently, and conditions later in the year may support even higher oil prices. However, a further rise could result in renewed drilling that would bring prices back down. Wherever they go, even steady oil prices could potentially lead to a modest increase in inflation by removing the mitigating impact that declining oil had over the past year.

The dollar has weakened somewhat in 2016, particularly against a rapidly rising Japanese yen, but it still remains up about 20% from the levels of mid-2014. Dollar strength presents a challenge to U.S. manufacturers, whose products are less attractive in foreign markets. We forecast a more stable dollar over the coming year, with moves up or down largely dependent upon the timing of the Fed's interest rate decisions. Although we expect inflation to remain tame, we also know the Fed will be watching closely and incorporating inflation trends into its plans for the next rate hike.

The net result of all of these factors is that analysts currently expect first quarter corporate earnings to decline about 8%. We expect actual results will come in slightly better than forecast, as they have for the past several quarters, but will still be weak. However, earnings should improve in the second half of 2016 as comparisons to last year become more favorable (energy sector woes began to hit hard last summer), and earnings should also be higher than 2015 for the full year as the economy continues to improve. Better earnings and reasonable current valuations – the market currently trades for a multiple of earnings (about 17) that is roughly in line with its historical average - provide support for higher stock prices.

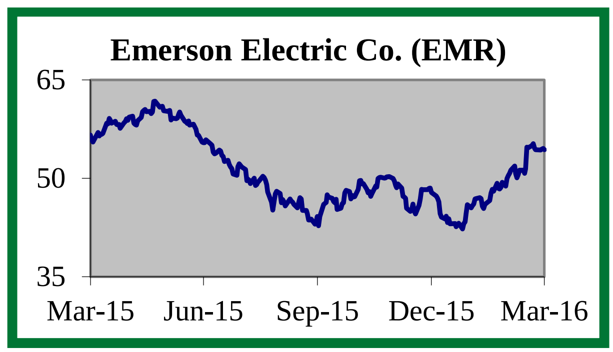
Introducing Our New Website

After much hard work and multiple photo sessions, we are proud to announce the unveiling of our new firm website. Please visit our site at www.edgemoorinv.com and share with your friends, but do not call us with comments on our pictures!

Analysis of Selected Securities

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

Emerson Electric Co. (EMR)



Past performance is not indicative of future results. Please see disclosures on page 8.

Price (3/31/2016)	$ 54.38	Forward P/E	16.0
Market Cap ($B)	$ 34.2	Price/Book	4.6
Dividend Yield	3.5%	Price/Sales	1.7
Return on Equity	29.9%		

Emerson Electric Co. (EMR) is a global leader in the design, manufacture, and sale of a broad range of electronic products, systems, and services for commercial, industrial, and consumer end-markets. The company's integrated industrial platform includes five operating segments: Process Management (37% of revenues, 44% of earnings), Industrial Automation (18%, 18%), Network Power (19%, 7%), Climate Technologies (17%, 20%), and Commercial & Residential Solutions (9%, 11%). Over half of the company's revenues are generated outside of the United

States, with its largest overseas markets in Asia and Latin America.

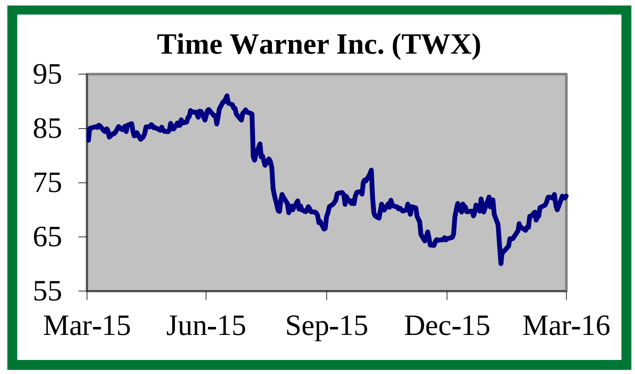
Emerson enjoys the distinction of being a "Dividend Aristocrat," meaning it is one of only 50 companies in the S&P 500 index that have raised their dividends every year for at least 25 consecutive years. In fact, the company's most recent dividend hike in the third quarter of 2015 represented the 59th straight year of such an increase.

The global slowdown in industrial production negatively impacted Emerson's 2015 results, as did the adverse currency effects of a strong U.S. dollar. In addition, the collapse of energy prices challenged Emerson's Process Management segment, where more than 40% of revenues are tied to oil and gas markets. But growth in the company's highly profitable Commercial & Residential unit partially offset these declines, while expected divestitures of some of the company's more commodity-like segments in 2016 will allow Emerson to refocus on servicing its most profitable customers.

In our view, Emerson's long history of generating high returns on equity and double-digit returns on invested capital speaks to the strength of its customer relationships and brand, the importance to customers of its products and services, and its overall size, scale, and cost advantages. These factors contribute to Emerson's wide economic moat and provide resiliency during periods of cyclical economic weakness.

Emerson also has a long track record of returning capital to shareholders through dividends and share buybacks, all driven by the company's strong free cash flow generation. We believe its overall financial position is strong, with $3 billion of cash on its balance sheet and total debt representing just 37% of total capital. With a forward price-to-earnings ratio of 16x and an attractive 3.5% current dividend yield, we believe this core industrial stock holds solid total return potential for investors.

Time Warner Inc. (TWX)



Past performance is not indicative of future results. Please see disclosures on page 8.

Price (3/31/2016)	$ 72.55	Forward P/E	12.3
Market Cap ($B)	$ 58.4	Price/Book	2.4
Dividend Yield	2.0%	Price/Sales	2.1
Return on Equity	15.9%		

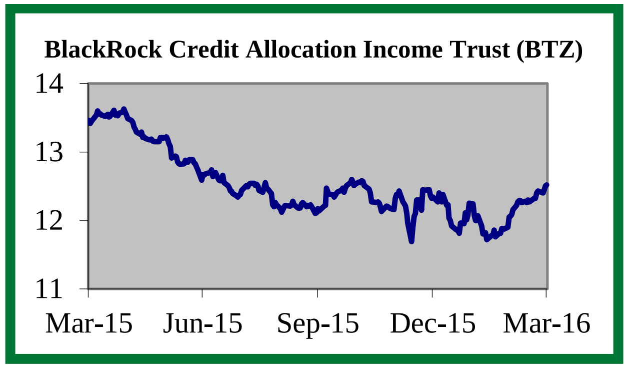
Time Warner Inc. (TWX) has become a pure-play entertainment business since its spinout of AOL and Time Warner Cable in 2009 and sale of the Time, Inc. publishing business in 2014. Today, the company operates three major entertainment segments: Turner Cable Networks (50% of consolidated earnings), HBO premium pay television (25%), and Warner Brothers Studios (25%). Its entrenched cable networks, including CNN, TNT, TBS, and HBO, and deep library of both old and new TV and movie content give Time Warner a wide economic moat and solid competitive advantages in the ever-changing media and entertainment business.

Time Warner's core cable business (CNN, TNT, and TBS) provides a steady stream of affiliate fees and advertising revenues, as these networks are among the most widely watched cable channels. Its premium cable channel, HBO, remains the prestige platform for exclusive original programming, and the newly launched HBO Now on-demand video streaming service is seeing fast growth among younger viewers.

Complementing these profitable cable platforms is Warner Brothers Studios, one of six major film studios and one of the largest producers of television content in the industry. Warner Brothers' film library includes classic films, recent box office hits, and movie franchises. The ever increasing demand for high-quality content from broadcast, cable, and streaming services translates into a steady source of cash flow and profits for Time Warner. Even as distribution methods for content continue to evolve and the potential migration of cable subscribers to the Internet or other delivery on-demand services remains a longer-term risk, pay-TV still dominates with penetration of about 90% of all U.S. households.

Financially, we believe Time Warner is on sound footing, with strong profitability, a solid balance sheet, and good growth prospects. Management has proven to be shareholder friendly, most recently announcing a 15% increase to its dividend in the fourth quarter and repurchasing $3.6 billion of its stock in 2015. With the stock trading at just 12.3x forward earnings and paying a steadily increasing dividend, Time Warner meets our criteria as a value-oriented holding with strong upside potential for investors.

BlackRock Credit Allocation Income Trust (BTZ)



Past performance is not indicative of future results. Please see disclosures on page 8.

Price (3/31/2016)	$ 12.52	Price to NAV	-9.8%
Fund Size ($B)	$ 1.5	Leverage Ratio	31.6%
Avg. Bond Rating	BBB	Dividend Yield	7.3%

The BlackRock Credit Allocation Income Trust (BTZ) is a closed-end fund that invests in a diversified portfolio of investment grade corporate and high yield bonds, bank loans, preferred securities, and convertible bonds. The fund's investment objective is to generate current income and capital appreciation for investors.

A closed-end fund differs from the more common open-end mutual fund in that shares are traded on an exchange, like an individual stock, with market participants acting as buyers and sellers. The fund itself does not issue or redeem shares daily. After its initial share offering, a closed-end fund's shares trade on the open market at either a premium or a discount to its initial selling price. Consequently, the fund has a stable capital base that the fund manager can invest without the need to hold or raise cash quickly to meet redemptions from investors.

We purchase BTZ for the income portion of client portfolios to obtain diversified income exposure managed by an experienced investment manager, BlackRock Inc. Over 80% of the fixed income securities held by the fund are issued by U.S. corporations, and 70% of the securities are rated investment grade by Standard & Poor's or Moody's Investor Services (BBB or better). The fund's largest sector concentration is in financial-related securities at about 24% of total assets, and its exposure to energy-related issuers stood at 17% of assets in 2015, which accounted for much of the stock's volatility last year. As with many closed-end funds, BTZ utilizes debt to expand its balance sheet and leverage its returns; its leverage ratio was 31.6% at year-end 2015.

BTZ currently trades at approximately a 10% discount to its net asset value and yields 7.3%. During the past three years, the fund has traded at between a 15% and 6% discount, with a three-year average of 10.9%. We believe BTZ provides diversified bond exposure for client portfolios with an attractive risk-adjusted return.

Source for charts and text: Morningstar, S&P, Schwab, Value Line, and Argus research 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 $775 million as of March 31, 2016 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.

Thomas P. Meehan – President
(301) 543-8881
tmeehan@edgemoorinv.com

Timothy C. Coughlin, CFP® – Managing Director
(301) 543-8371
tcoughlin@edgemoorinv.com

R. Jordan Smyth, Jr., CFA – Managing Director
(301) 543-8370
jsmyth@edgemoorinv.com

Paul P. Meehan, CFA – Managing Director
(301) 543-8373
pmeehan@edgemoorinv.com

Gay S. Truscott, CFP® – Senior Vice President
(301) 543-8375
gtruscott@edgemoorinv.com

Christine J. Potts – Vice President
(301) 543-8365
cpotts@edgemoorinv.com

Sara R. Parker – Vice President
(301) 543-8363
sparker@edgemoorinv.com

Anne Baker – Executive Assistant
(301) 543-8366
abaker@edgemoorinv.com

Suite 315
7250 Woodmont Avenue
Bethesda, MD 20814
(301) 543-8358 fax

www.edgemoorinv.com
www.edgemoorblog.com

Past performance is not indicative of future results. The information provided in this report should not be considered financial advice or a recommendation to buy or sell a particular security. There is no assurance that any securities discussed herein will be included in or excluded from an account's portfolio. The securities discussed may not represent an account's entire portfolio and in the aggregate may represent only a small percentage of an account's portfolio holdings. It should not be assumed that any of the securities transactions discussed were or will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein. Edgemoor Investment Advisors, Inc. reserves the right to modify its current investment strategies and techniques based on changing market dynamics or client needs. All recommendations for the last 12 months are available upon request.

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 is discussed for comparative purposes only. The comparison has limitations because the index has volatility, investment, and other characteristics that differ from the investment strategies of Edgemoor. Further, it is not possible to invest directly in the index.

Edgemoor Investment Advisors, Inc. is an independent investment adviser registered under the Investment Advisers Act of 1940, as amended. Registration does not imply a certain level of skill or training. More information about Edgemoor Investment Advisors, Inc. including our investment strategies, fees, and objectives can be found in our ADV Part 2, which is available upon request.