EDGEMOOR
INVESTMENT ADVISORS

Edgemoor's Quarterly Report

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A Promising Start

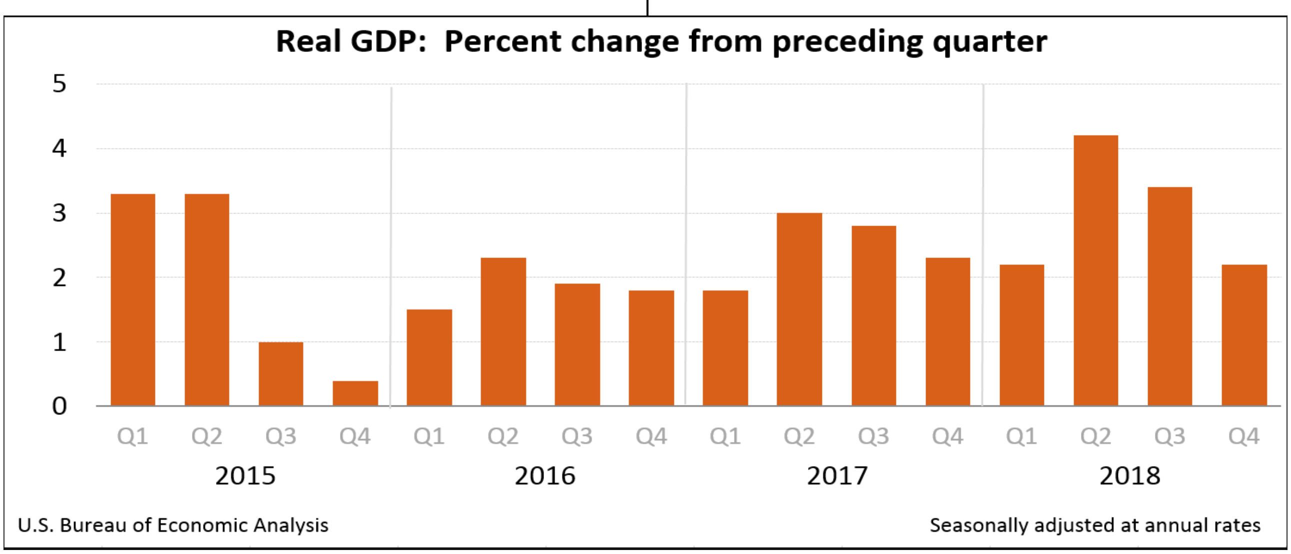
What a difference a quarter makes. The U.S. stock market rebounded sharply in the first quarter of 2019, posting its best start to the year since 1998. This outstanding showing came after a dismal end to 2018 and eased fears of an imminent end to this long-running economic recovery and bull market.

Economic growth, trade, corporate earnings, central bank policy, and political matters remain at the forefront of issues investors are watching at home and abroad. We are optimistic that the market can hold, and perhaps add to, its gains. However, we expect to see more volatility along the way.

First Quarter Review

The market's rebound from December's dive began after Christmas, when investors decided that the selloff was overdone, given signs of ongoing economic growth and much lower stock valuations. The S&P 500 index rose throughout the first quarter and delivered a total return of 13.6%. Bonds also moved higher, with the Bloomberg Barclays U.S. Aggregate Bond index returning 2.9%, as yields moved lower due to continued low inflation and signals from the U.S. Federal Reserve Board that it would likely not raise the federal funds rate further this year.

Economic indicators were mixed and generally confirmed that the U.S. economy continued to expand, despite the partial government shutdown, though at a slower rate than in previous quarters. U.S. gross domestic product (GDP) rose 2.2% in the fourth quarter of 2018, solid growth but lower than the 3.4% and 4.2% in the third and second quarters, respectively.



Past performance is not indicative of future results.

Jobs growth in January (312,000 additions) and March (196,000) was consistent with the results over the past several years, though February's number (revised to 33,000) was unusually weak and appears to have been an anomaly. Unemployment stayed low at 3.8%, and inflation remained below the Fed's target rate of 2% despite wage growth of 3.2%. Consumer confidence remained high but dropped slightly in the face of the partial government shutdown, the disappointing February jobs report, and other signs of moderating economic growth.

Fed policy was the center of attention during the quarter, and comments from the Fed revealed greater wariness of factors hindering economic growth. In addition to pausing on interest rate increases, the Fed also announced its intention to stop reducing the size of its vast bond portfolio in September of this year. The yield on the 10-Year Treasury was 2.4% at the end of the quarter, down from 2.7% at the beginning.

In addition to watching the Fed's statements and actions, investors also closely monitored bond yields for clues regarding economic growth. A brief yield curve inversion at the end of the quarter momentarily spooked markets, as short-term interest rates rose above long-term rates and signaled expectations of economic weakness. The inversion did not last long enough to serve as a strong warning, but it did renew talk of a potential recession.

Trade threats and talks continued during the quarter, with the feud between the United States and China getting most of the attention. The Brexit negotiations and votes in the U.K. Parliament did little to quell the uncertainty surrounding Britain's looming exit from the European Union. Meanwhile, many businesses are making changes out of concern that the trade wars will not end soon and, even if they do, are fundamentally altering the global landscape. In one shift, some manufacturers have moved production and sourcing out of China to Vietnam and other Asian countries.

As reported in the first quarter of this year, earnings rose again in the fourth quarter of 2018, fueled by a combination of strong business fundamentals and lower tax rates. However, the earnings growth of 13.3% was slower than the average rate of 25.3% in the first three quarters of 2018, and business leaders are keeping a wary eye on trade issues and Fed policy as they plan for future investment.

Outlook for the Rest of 2019

Having nearly recovered to its September 2018 peak, the S&P 500 index may hover near its current level for a while as investors digest upcoming earnings reports and assess overall economic and political conditions. We currently expect more gains for stocks by the end of the year, given reasonable valuations and our expectations for moderate earnings growth, but stock performance will depend not just on reported earnings but also the outlook provided by management.

As usual, Fed policy will have a significant influence on the economy, the markets, and overall consumer and investor sentiment. Most likely, in our opinion, is a scenario including low bond yields, modest inflation, and GDP growth of about 2% annually, a combination that should allow the Fed to stand pat and stocks to hold their gains and even rise a bit further through year end.

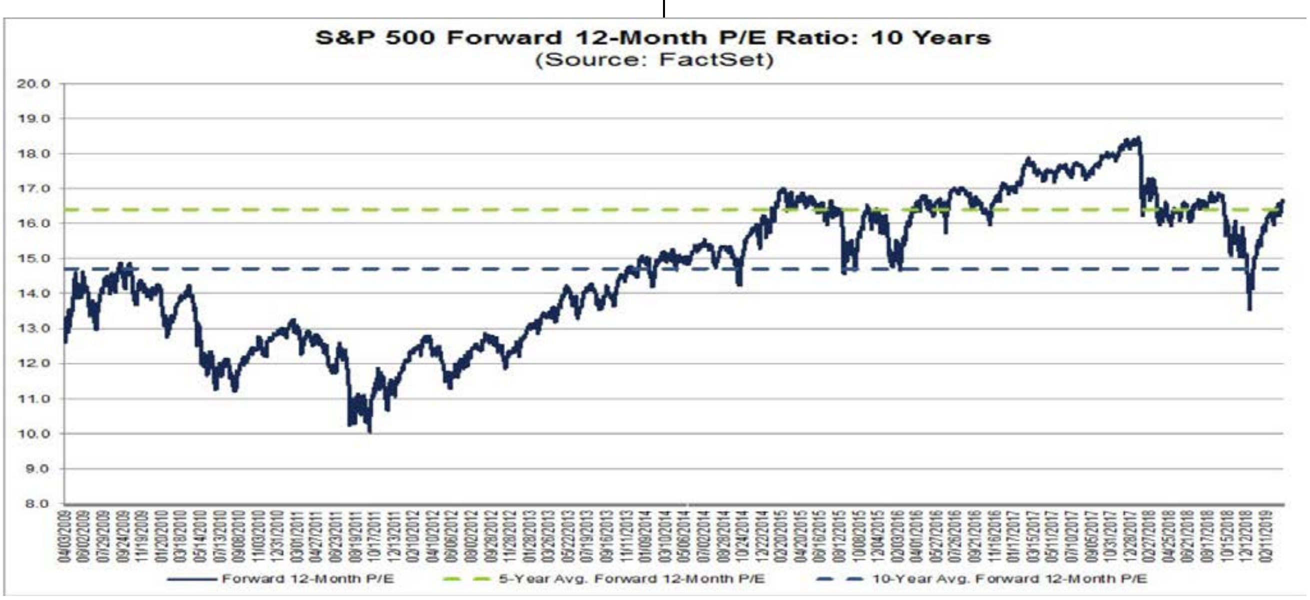
We currently see little risk of recession in 2019, given our assessment of economic conditions, but a surprise one way or another regarding employment, inflation, or the direction of interest rates could bring a sharp reaction from the markets.

Government policy and action related to trade and geopolitical issues will continue to attract focus from investors. We are optimistic that U.S. government leaders will find a way to agree with China and other global trading partners on just enough change to address the most important issues and then move on, stopping short of either a protracted and damaging trade war or a comprehensive solution that achieves all administration goals. The third year of a presidential term is usually good for the markets, since the White House wants to do whatever it can to boost the economy heading into the next year's elections. This historical trend gives us confidence and hope that the current administration will realize that a quick resolution of trade issues is in its own best interests.

U.S. corporate earnings, due out in the next several weeks, will likely fall for the first quarter, partly due to the prolonged government shutdown and trade wars. Analysts currently expect a year-over-year drop of about 4.2% in S&P 500 earnings in the first quarter and relatively flat earnings in the second, followed by a resumption of earnings growth in the second half of this year and a full-year 2019 increase of about 3.5%.

Looking abroad, we see uneven growth prospects, with European countries struggling to prolong economic expansion and easing monetary policy while facing the uncertainty and looming impact of Britain's exit from the European Union. China is similarly wrestling with the best mix of policies to boost its economy, though growth rates there and in other emerging markets are already significantly higher than in most of the developed world. We still see opportunities for good long-term investment in foreign markets, given relatively low valuations that we believe offset the mixed economic outlook. We expect emerging markets, in particular, to offer solid returns over the coming years as more consumers in those countries gain the means to participate in the local and global economies.

The S&P 500 index is now trading for 16.7 times projected earnings for the next year, roughly in line with its historical average.



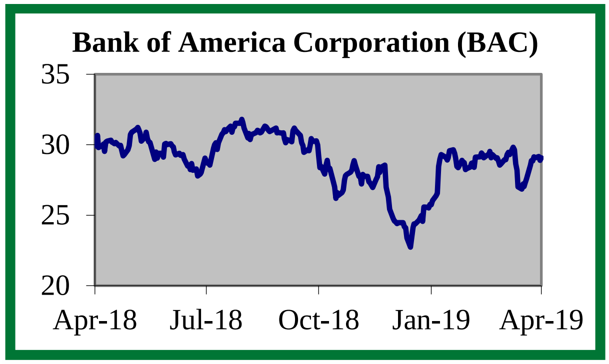
Based on this and other measures of market valuation, we believe the broad market is neither overvalued nor undervalued. Keep in mind that we purchase and hold in our portfolios a small subset of the market, and we believe each of the securities we own is currently trading for less than our estimate of its intrinsic value, the price we believe it should reach as the market fully values the company's prospects.

For the income portion of our portfolios, we still see good opportunities to invest in high-yielding equities and have added some bonds to our portfolios to help provide stability in times of market uncertainty. We continue to invest the majority of our income portfolios in utilities, pipeline companies, preferred stocks, and other equities with higher yields than currently offered by bonds. In our opinion, many of these securities should also be able to increase their payouts over time, providing a hedge against inflation and the potential for price appreciation.

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 market today.

Bank of America Corporation (BAC)



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

Price (04/10/2019)	$29.07	Forward P/E	10.1
Market Cap ($B)	$280	Price/Book	1.2
Dividend Yield	2.1%	Price/Sales	3.3
Return on Equity	11.0%		

Bank of America is one of the largest financial institutions in the world, with total assets of more than $2.3 trillion, deposits of nearly $1.4 trillion, and a market capitalization of $280 billion. Bank of America operates a network of 4,000 branches and 18,500 ATMs, and it has 24 million online banking customers, more than one-third of all online banking customers in the United States. In addition, B of A has operations in over 30 countries worldwide.

The bank operates in four business segments: Consumer Banking, Global Wealth and

Investment Management, Global Banking, and Global Markets. Consumer Banking, the largest segment, generates approximately 45% of the bank's total revenues and net earnings and is ranked first in consumer deposit market share among U.S. banks. Global Wealth Management, with more than $2.6 trillion in assets under management, also holds the top market position in client assets, trust assets, and loans.

Since the global financial crisis of 2008-2009, Bank of America has remade itself by shedding assets, building capital, and improving credit quality and systems. Management has also adopted a "responsible growth" strategy to expand loan portfolios without taking on undue credit risk or relying on volatile segments like trading and investment banking to drive profits. The plans are coming to fruition, with the bank's Tier 1 capital ratio rising to 11.9% as of December 31, 2018 and non-interest expenses declining sharply. Bank of America now spends just 58.5 cents to generate every new dollar of revenue, down from 88 cents in the aftermath of the financial crisis.

As B of A has returned to financial health, the Federal Reserve has allowed the bank to steadily increase the capital it returns to shareholders. In 2018, these payouts totaled $25.5 billion, comprised of $5.4 billion in dividends and $20.1 billion in share repurchases. By contrast, in 2014 the bank was permitted by regulators to return just $2.9 billion to shareholders between dividends and buybacks.

Bank of America is one of the few banking institutions to carry a wide economic moat - a measure of competitive strength - according to independent research firm Morningstar. This wide moat comes from the bank's low-cost deposit base and sustainable cost advantages, as well as its breadth of products and services that offers customers a true one-stop shop of financial services, increasing loyalty and resulting in high switching costs. The bank also benefits from economies of scale in areas like credit card issuance and mortgage lending, two areas in which B of A is a dominant player and can spread the fixed costs of these operations across a large platform of customers.

We believe Bank of America shares are attractively valued at 10.1 times 2019 earnings estimates, below the five-year average and most of the bank's peers. In addition, the bank pays a dividend that we expect to grow steadily as management increases the payout ratio from the current 23% to the stated goal of 30% of earnings. Overall, we believe that Bank of America is well positioned to grow its earnings as the credit and regulatory issues of the financial crisis recede and its restructuring efforts continue to pay off.

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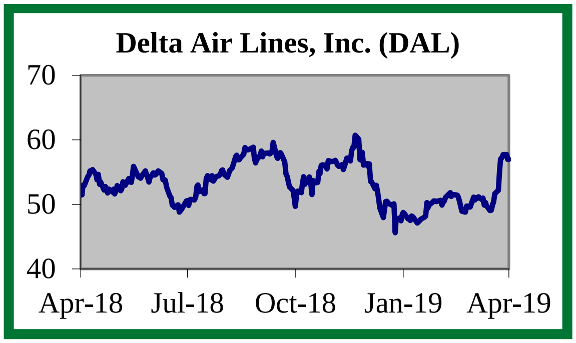
Delta Air Lines, Inc. (DAL)



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Price (04/10/2019)	$57.86	Forward P/E	8.6
Market Cap ($B)	$39.8	Price/Book	2.8
Dividend Yield	2.4%	Price/Sales	0.9
Return on Equity	28.5%		

Delta Air Lines is a major international airline and the largest U.S. carrier by market capitalization. Its U.S. presence includes hubs in Atlanta, Boston, New York, Detroit, and Minneapolis. Delta generates 84% of its revenues from passenger travel, 2% from cargo, and 14% from other sources. The carrier generates 71% of revenues in the United States, 15% from Atlantic routes, 7% from Pacific routes, and 7% in Latin America.

Delta's major U.S. hub is Atlanta's Hartfield-Jackson airport, the world's busiest, where the airline has a commanding 73% market share, the highest market share for any U.S. carrier at a hub location. 40% of Delta's network routes go through Atlanta, a route structure that results in higher densities, lower costs, and industry-leading revenue per available seat mile. Delta's highly efficient route operations have allowed the airline to consistently generate operating margins and returns on assets and equity that exceed peers.

Delta uses no Boeing 737-MAX jets in its fleet, so it is not exposed to the disruption related to the recent grounding of that plane model.

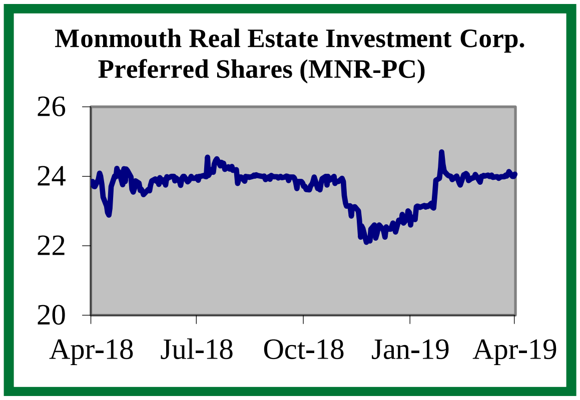
Delta's expanding global operations include partnership in the SkyTeam global alliance as well as joint ventures with international carriers like Air France-KLM, Alitalia, and Virgin Atlantic. Growth in international air travel is expected to outpace growth in the more mature U.S. market.

Delta also runs a highly profitable SkyMiles loyalty program, which generates 60% operating margins and contributes nearly 30% of the airline's operating income. Just this month, Delta renewed its lucrative SkyMiles agreement with American Express, extending the relationship through 2029. The new agreement should deliver an incremental $3 billion to shareholders, or roughly $4 per share, and Delta shares rose 6% on the day the deal was announced.

Delta is financially strong and shareholder-friendly. The company carries an investment grade credit rating from all three major agencies and generates strong cash flows, which enabled management to increase the dividend 15% and repurchase $1.6 billion of its shares in 2018.

Delta shares trade at 8.6 times 2019 earnings estimates and offer an attractive 2.4% dividend yield. Delta should continue to benefit from strong industry fundamentals, moderate capacity growth, growing ancillary revenues, and steady demand for air travel, as reflected in its 5-year projected earnings growth rate of 11%.

Monmouth Real Estate Investment Corp. Preferred Shares (MNR-PC)



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

Price (04/10/2019)	$24.06	Par Value	$25.00
Market Cap ($B)	$1.3	Dividend Yield	6.4%
Preferred Coupon	6.1%		

We purchase a variety of income-generating securities for clients' income portfolios, including preferred stocks. We like preferred shares because they offer attractive yields, typically in the 5%-6% range, that provide a buffer to rising interest rates. They also act as a counterweight to the shorter-term, lower-yielding bonds and bond funds which we buy in clients' portfolios, creating a barbell effect in terms of duration.

Most of the preferred shares we have purchased over the years are in the banking and real-estate sectors. One such preferred share which we are currently buying is issued by Monmouth Real Estate Investment Corp. Monmouth owns and manages high-quality industrial buildings generally located near major e-commerce hubs. The company's buildings are typically modern, single-tenant facilities leased under long-term agreements to tenants with strong credit.

As of December 31, 2018, nearly 99% of Monmouth's properties were leased, and 80% of its tenants, including its largest tenant FedEx, carried investment grade credit ratings. In addition to FedEx, Monmouth's tenant roster also includes high quality companies like Amazon, Coca-Cola, and Anheuser-Busch. Funds from operations, a widely used performance measure for real estate investment trusts, has grown steadily in recent years as management has successfully executed on its growth through acquisition strategy.

These Monmouth preferred shares pay an annual fixed-rate dividend of $1.53 per share that results in what we consider to be a very attractive current yield of 6.4%. The shares have no fixed maturity date but can be called by the company at any time at their par value of $25 per share, a premium to their current price. Monmouth's business model should continue to generate stable, predictable cash flow that comfortably covers its preferred dividend.

Source for text: Morningstar, S&P, Schwab, ValueLine, Black Diamond Performance Reporting, Yahoo Finance, 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 $960 million as of March 31, 2019 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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