

## Alley Company Dividend Portfolio 2022 Q4 Letter

January 20, 2023

The big story in 2022 was inflation and its broad effects on the economy. Whether it be burdening consumers with higher food and energy costs, challenging corporate America to manage higher cost pressures and end-product pricing, or forcing the Federal Reserve to quickly and aggressively tighten monetary policy, inflation had everybody's attention.

As the Fed raised interest rates to fight inflation, financial markets endured a challenging year. Looking ahead, however, tighter monetary policy and improving supply chains will hopefully moderate inflation pressures. With that in mind, there are some favorable trends that have recently developed:

- After peaking at a 40-year high of +9.1% in June, the consumer price index (CPI) annual rate has declined to +6.5% as of December.
- The monthly CPI statistics from July through November show a material easing of inflation down to an annualized rate of +2.6%.
- The prices of crude oil and natural gas have declined by 35% and 55%, respectively, since June.
- Fourth quarter 2022 wage growth on an annualized basis came in at +4.1% compared to +6.1% a year ago.

To be sure, the Fed's resolve to tame inflation could result in recession and will likely slow earnings growth in 2023. But the more important question in our mind for long-term oriented investors is: what will earnings be a few years out? To that end, we continue to seek out quality companies for the portfolio that have enduring businesses and astute management teams.

In our estimation, high-quality dividend payers continue to be a favored investment vehicle for the long-term growth of one's purchasing power. Companies that exhibit the ability to sustain and grow dividends typically have positive fundamental attributes including strong cash flow characteristics and healthy balance sheets.

### Quarterly Performance Update

During the fourth quarter of 2022, the Alley Company Dividend Portfolio outperformed the Russell 1000 Value Index benchmark. For the full year, the portfolio outperformed the benchmark in a down market which is consistent with our 5-year downside capture ratio of .89.

Stock selection was the primary driver of outperformance for the year with holdings in energy, health care, and industrials leading the way.

From an individual holdings perspective, top contributors to and detractors from performance in the portfolio during the fourth quarter were:

<b><u>Top Contributors</u></b>	<b><u>Top Detractors</u></b>
Phillips 66 (PSX)	Apple (AAPL)
BlackRock (BLK)	Crown Castle (CCI)
Merck (MRK)	Medtronic (MDT)

Top and bottom performing sectors in the marketplace during the quarter are displayed in the table below.

<b><u>Top Performing Sectors</u></b>	<b><u>Bottom Performing Sectors</u></b>
Energy (+/-)	Consumer Discretionary (+/-)
Industrials (+)	Communication Services (-)
Materials (-)	Real Estate (+/-)

(+) indicates that the portfolio is overweight this sector and (-) indicates that the portfolio is underweight this sector relative to the benchmark.

There were no portfolio changes made during the fourth quarter. The full year 2022 portfolio turnover ratio was 4%, which highlights our tax-efficient management and the long-term mindset of our investment philosophy. Since inception, the portfolio turnover ratio is 14%.

Dividend announcements among Alley Company Dividend Portfolio holdings during the fourth quarter were:

<b><u>Company</u></b>	<b><u>Dividend Change</u></b>
Abbott Labs (ABT)	9%
AbbVie (ABBV)	5%
Amgen (AMGN)	10%
Crown Castle (CCI)	6%
Merck (MRK)	6%
Snap-On Inc. (SNA)	14%

For the calendar year 2022, the *average* dividend increase announcement from our portfolio holdings was approximately +8.5%. We view this experience positively and an indication of favorable underlying bottom-up fundamentals. With elevated inflation trends, strong dividend growth can help investors maintain or increase purchasing power.

## **Alley Company Dividend Portfolio**

The investment philosophy of the Alley Company Dividend Portfolio focuses on striking the balance between attractive absolute dividend yield and strong dividend growth underpinned by solid company fundamentals of our portfolio holdings. We employ a bottom-up, research-driven process focused on fundamental analysis of our portfolio holdings.

## **Alley Company**

Alley Company is a boutique investment management firm that is dedicated to operating a discernible and disciplined investment philosophy and generating superior risk-adjusted investment returns. Alley Company was founded in 1998 and in 2006 established the Alley Company Dividend Portfolio to capitalize on investment opportunities in quality companies with strong dividend-paying cultures.

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