

Brookmont Capital Management

Dividend Equity Strategy – First Quarter 2010 Review

“Return of the Dividend”

Stocks that pay quarterly dividends have suffered these past two years as many companies were forced to reduce or eliminate their quarterly payments. The sheer amount of reductions in 2008 shook investor confidence in dividend-paying stocks and came when the general market was in a fast retreat. Always considered to be a safe-haven during a bear market, dividend-paying stocks fell just as hard as the rest of the market and have recovered at a slower pace over the past twelve months.

That said there seems to be a growing investor demand for dividend stocks: their valuations remain lower than the market averages, many investors are liquidating the names that led the market in 2009, and companies are beginning to boost their quarterly dividend payouts. According to Standard and Poor's, 399 of 7,000 reporting companies boosted its dividend during the first quarter of 2010 while only 48 companies either reduced or eliminated its dividend. That compares to 367 companies that reduced or eliminated its dividend during the first quarter of 2009 and 83 during the first quarter of 2008. However, with more than 1,400 negative dividend actions in 2008-2009 it will take some time until dividend payouts equal the levels seen in 2007. Too many companies remain concerned about the health of their business, as well as the economy, and are content on building a large cash allocation.

Dividend-paying stocks have badly trailed the S&P 500 over the past twelve-months and two-years, however, that underperformance might be seeing a change as well. As bond yields remain at historic lows, and yields are non-existent in short-term investments, a stock that is currently yielding 4% with the potential to grow the quarterly dividend as well as offer capital appreciation, is beginning to catch investor's attention. It also helps that the market rally is moving into its next cycle and should benefit several sectors that include dividend-paying stocks (including Health Care, Industrials, and eventually Energy).

The Dividend Equity Strategy has benefitted from the rising demand in dividend stocks and helped it outperform the major indices (S&P 500, Dow Jones, and Nasdaq) during the first quarter. Sectors that paced the Strategy's performance include Industrials, Materials, and Financials while the laggards included the Health Care, Telecom, and Utility sectors. The Strategy's sector performance rankings were very similar to the S&P 500 during the first quarter.

One new holding was added to the Strategy during the quarter (United Parcel Service) and no existing holdings were liquidated. This trade brings the Strategy's cash weighting down to 1% of the total portfolio. The Strategy's market-cap weightings remain unchanged at 56% large-cap and 44% in mid and small-cap equities. We are not forecasting any significant changes to the Strategy's holdings during the second-quarter of 2010 unless we see a significant shift in the U.S. economy. Stock prices are approaching full valuation and the first-quarter has already provided 50% of our forecasted total return for the year. That does not mean we will not find new opportunities as the year progresses; it means that they will be harder to find and fewer to choose from.

Morningstar Rankings

According to Morningstar's database of Separate Managed Accounts, the Dividend Equity Strategy's total return ranked within the top 5% of its category (Large Cap Value) in 2008 and within the top 7% of its category in 2009.



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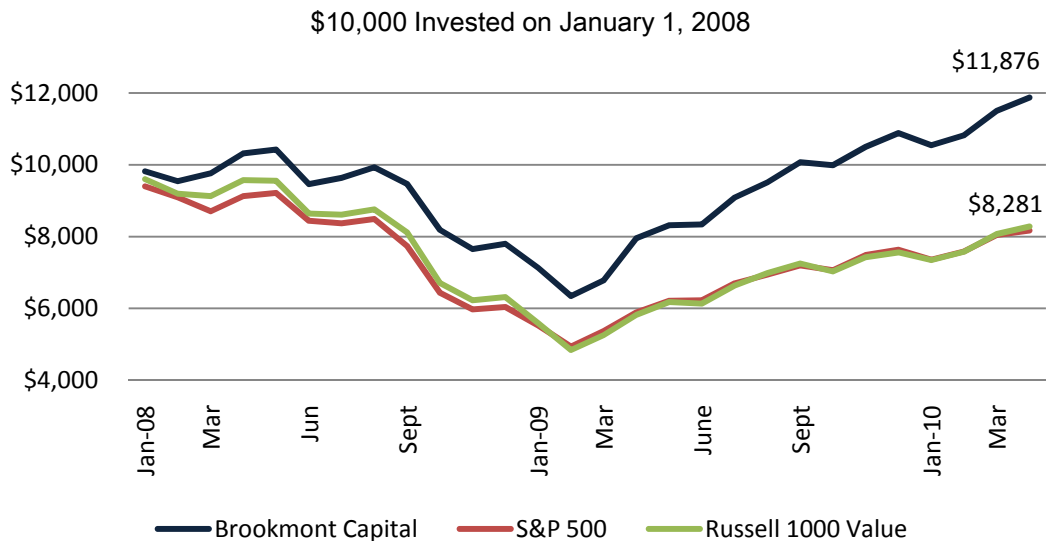
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The Strategy versus the Russell 1000 Value Index

The Strategy's true benchmark has always been the Russell 1000 Value Index. It consistently has the highest correlation with the Strategy and its universe of 677 names includes the majority of our holdings. However, it is important to remember that the Strategy has a strict restriction that any new holding must provide at least a 3% current yield. That one important hurdle reduces the number of qualifying names in the Russell 1000 Value down to 117. The Strategy currently owns 11 of the qualifying names and drops the list down to 106. When you consider that many of the remaining names are very similar to our current holdings (i.e. Pepsi versus Coca-Cola), the qualified list of names drops by 36 down to 70. Since we have made the decision to use an Exchange Traded Fund for our REIT exposure, it eliminates another 29 names from our qualified universe.

Very quickly our universe has dropped from an initial 677 names down to only 41. When we screen the remaining names through our top-down analysis, followed by an additional nine quantitative hurdles, the universe is narrowed down to roughly 15-20 individual stocks. Since the Russell indices do not include foreign stocks, we are able to add about 20 names to our universe. The Strategy is not bound to only value stocks and allows the universe to include certain holdings from the Russell 1000 Growth Index as well. In the end, our universe will include close to 55 equities that we do not currently own, are not a Real Estate Investment Trust, and is not a close equivalent to a current holding.

This multiple screening process allows efficient management of the Dividend Equity Strategy where we focus on a very select number of potential holdings. It also translates into a lower annual turnover and longer holding periods.



Disclosure – returns do not include management fees but do include transaction costs. Returns for the Dividend Equity Strategy are based on a composite of discretionary accounts that own all Strategy holdings. Strategy returns do not assume reinvestment of dividends or capital gains. Past performance is no guarantee of future results and this information is for presentation purposes only. Returns for the benchmarks assumes that income and capital gains are reinvested. It is not possible to directly invest in an Index.