DVI

David Vaughan Investments

DVI Update

05/11/2020

At DVI, we began to set the wheels in motion in mid-April to develop and implement a return-to-office (RTO) plan effective June 1st. Despite the fact that in Illinois, Governor Pritzker had elected to extend and modify the shelter-in-place executive order through the end of May, it was clear to our leadership team that it was time to think through the necessary steps to bring our associates back to our physical office locations. In doing so, we have also come to recognize the ongoing necessity of a parallel path, one in which includes a permanent work-from-home workforce strategy. As we execute our RTO plan, starting with 60% of our workforce and working towards 80% in full implementation status, we have never lost sight of our number one priority, the safety and well-being of our colleagues and their families.

Unfortunately, despite the fact most DVI associates will be back working in their offices, we recognize, at least at the outset, that we have yet to return to an environment that would be characterized as "business as usual." Client and strategic partner interactions will continue to be limited to voice and video conference calls, and even internal meetings will be held for the most part utilizing our Teams technology. There is no question that we would all like to turn back time on all of this, but rather than reminisce about the past, we have elected to establish a path to move forward in a positive way for all DVI stakeholders.

An Impactful Perspective

Imagine you were born in 1900:

- On your 14th birthday, World War I began and ended on your 18th birthday. 8.5 million people perished in that war, and Allied and Central Power countries experienced total casualties of nearly 37.5 million.
- Later in the year, the Spanish influenza pandemic hits the planet and runs until your 20th birthday. It is estimated that 25 million people died from it, though some researchers have claimed the death toll to be between 40 and 50 million.
- On your 29th birthday, the Great Depression begins. Unemployment in industrialized countries hits 25%, GDP in the United States declines by 30% and industrial production falls by 46%. That runs until you are age 33.
- When you turn age 39, World War II starts. On your 41st birthday, the United States is fully pulled into WWII. Between your 39th and 45th birthday, as many as 50 million people perish in the war.
- Smallpox was an epidemic until you were in your late 40's, and the global death toll from the variola virus during the twentieth century has been estimated to be nearly 300 million.
- At age 50, the Korean War starts. By age 53, nearly 5 million troops and civilians are dead, wounded or missing.
- From your birth, until reaching your mid-50s, you faced the fear of Polio epidemics each summer. You experienced friends and family being either paralyzed or dying from the disease.
- At age 54, the Vietnam War begins and doesn't end for nearly two decades. As many as 3.5 million people perish in that conflict.
- On your 62nd birthday you have the Cuban Missile Crisis, a tipping point in the Cold War. For those 13 days in October, life on our planet as we knew it, almost ended.

It is hard to imagine that anyone could survive through all of this let alone thrive, but they did. Think of your parents, grandparents or great grandparents who endured through significant tragedy and turmoil. Despite the considerable challenges that we face today with the Covid-19 pandemic and the economic fallout caused by it, history proves out that the human condition tends to rise to the occasion and overcome adversity. We must all lend a helping hand to others and keep things in perspective.

(Excerpts from recent e-mail correspondence and referenced statistics validated)

DAVID VAUGHAN INVESTMENTS

Market Insights

Market Valuation

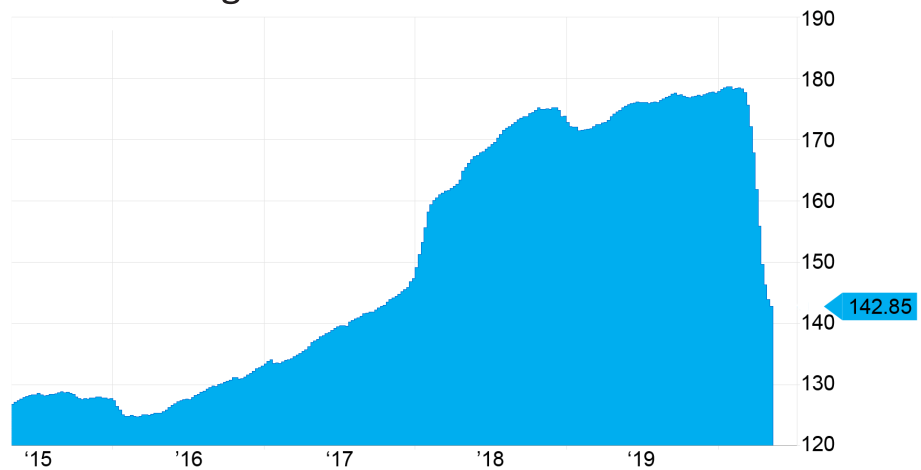
Since the March 23rd lows, the S&P 500 Index has experienced a recovery from high to low of nearly 35%. Quite a remarkable rebound in the face of economic indicators that are suggesting that the economy is contracting at a pace not seen since the Great Depression. The magnitude of economic uncertainty is such that most companies are no longer providing earnings guidance for next quarter, let alone for the balance of the year. Charlie Munger, Warrens Buffet's 96-year-old side kick made recent comments in a Wall Street Journal interview that were quite revealing. For someone that has seen and experienced more than most, Charlie remarked, "This thing is different. Everybody talks as if they know what's going to happen, and nobody knows what's going to happen."

S&P 500 Index

Source: FactSet

As the market has recovered over the past weeks, forecasted earnings for S&P 500 companies have been in a steep decline. Full Year 2020 earnings that were projected at nearly $ 180 back in early February are now forecasted to come in around $ 140 per share or a decline of nearly 22 percent. And remember, based upon the lack of forward visibility, these estimates are going to be subject to significant revisions in the coming months.

Earnings Per Share - Next Twelve Months



Source: FactSet

With prices rising and earnings falling, Price/Earnings (P/E) ratios have been on the rise. P/E ratios are now running in excess of 20 times forward earnings, nearly 25 percent higher than the long- term average. It really has been a game of catch up. Back in mid-March, as prices were near their bear market lows, analysts had yet to mark down earnings in any material way. The earnings decline is now well entrenched, but now the stock market is looking forward and is more optimistic about future economic activity.

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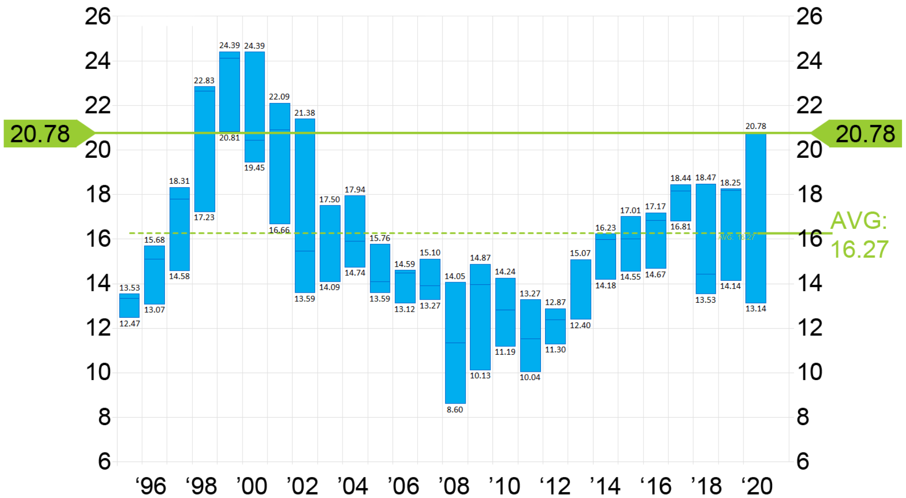
Market Valuation



Source: FactSet

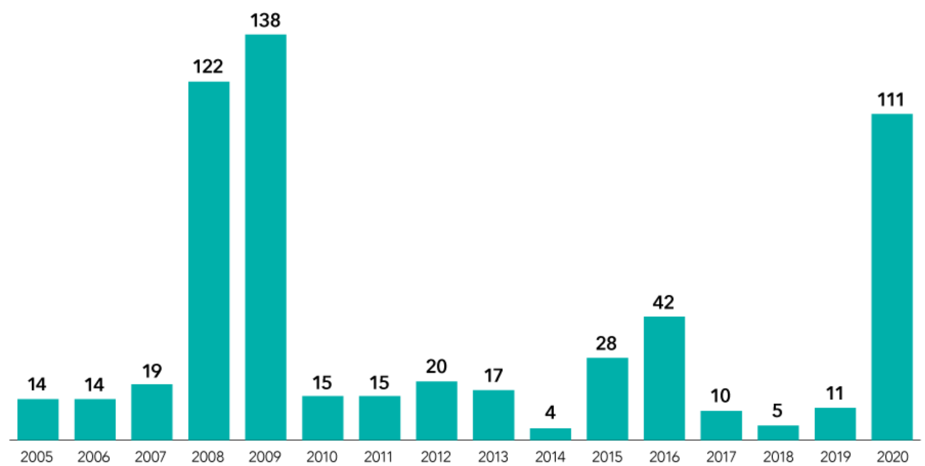
The Importance of Dividends

In a market and economic environment ripe with uncertainty, we continue to place a great deal of importance on dividends. Now more than ever, we believe most investors will be seeking out companies that will not only be able to weather the storm but also provide current cashflow through the payment of dividends. Unfortunately, with corporations viewing cash and liquidity as their top priority, dividend payments cannot be taken for granted. For most companies, the suspension of their share re-purchase program is step one and a dividend reduction or payment suspension is a clear number two.

DVI places a great deal of research significance on a company's ability to generate reliable cashflow. In addition, we are constantly evaluating the consistency of earnings and the sustainability of the company's business model. In the current environment, we are trying to be as opportunistic as possible to increase the quality of our holdings while not having to pay valuation multiples outside of our value-oriented mandate. Industry diversification also plays a key role in our portfolio strategy, making sure we do not have all eggs in just one basket.

Dividend Cuts or Suspensions

Number of U.S. companies that have cut or suspended dividends



Source: Capital Group

The unprecedented nature of the current healthcare and economic crisis certainly contributes to the challenge of maintaining portfolio dividend yields that are not only attractive, but dependable as well. Though we know we will once again be put to the test, we are confident that DVI is up to the challenge.