SUMMER 2018 ISSUE

Donaldson CAPITAL MANAGEMENT

RISING DIVIDEND REPORT

Security ▪ Income ▪ Growth ▪ Service

QUARTERLY
QUICK FACTS

When will the bull market end?

DCM uses a test of eight indicators that flashed warnings as the end of the 2000 and 2007 bull markets approached. Using this test, we predict that barring any shocks to the U.S. economy, the current bull market should continue.

Only one of the warnings is present today.

1. Extreme valuations – No
2. Speculative buying – No
3. An increase in IPOs – No
4. Rising interest rates – Yes
5. Weakening earnings – No
6. Eroding market breadth – No
7. Defensive sectors leading – No
8. Widening credit spreads – No

In 2000, all indicators pointed to Yes; and in 2007, all but one indicator pointed to Yes. While we do expect to see more volatility over the next few months, underlying economic and business fundamentals are strong.

2018 — Pack Your Patience

What a difference six months can make

Kyle Markle

Joe Zabratanski

IF 2017 WAS BEST categorized by low volatility and a lack of market moving news events, 2018 has proven to be just the opposite, so far. While the year began with the best January on record the market quickly turned lower on the heels of higher than expected wage inflation and subsequent trade war talk.

As the year has progressed, there has been no shortage of noise. Headlines, news events, and tweets have investors and traders alike more fearful than at any point in 2017. These periods of instability can be painful to live through, but corrections are a very necessary part of a healthy bull market.

Mixed within all of the negative headlines, strong data on the U.S. economy and corporate earnings growth recently have been bright spots in an otherwise conflicted market. Preliminary estimates for the 2nd quarter U.S. GDP are coming in at levels not seen since 2012. In addition, 1st quarter earnings and sales growth of nearly 25% and 8%, respectively, are as strong as we have witnessed in recent memory. Without an accompanying increase in stock prices, the market is now more attractively valued than at the beginning of the year.

Much of this allows us to draw parallels between 2018 and the equity markets of 1984 and 1994. While there are never perfect comparisons, both of those periods also saw above average GDP and earnings growth, yet the equity market zig zagged for much of those years. Perhaps most encouraging to us is that equity markets were up over 25% in the year following these "transformational" years. There certainly are differences between the periods, but it is easy to see how 2018-2019 could unfold in a similar fashion.

With trade negotiations ongoing as well as the summer months and midterm elections still to come, we advise **packing your patience** as it wouldn't be surprising to see more of this back-and-forth market to continue. Our dividend growth strategy has held up through different types of markets and regardless of what the remainder of 2018 has in store, we believe that our security, income, and growth objectives are positioned to serve you well.

Kyle
KYLE MARKLE
CHIEF INVESTMENT OFFICER &
SR. PORTFOLIO MANAGER

Joseph P. Zabratanski
JOE ZABRATANSKI
CHIEF INVESTMENT OFFICER &
SR. PORTFOLIO MANAGER

Charitable Giving STRATEGIES for Today's Tax Laws

You may need to reconsider your approach to charitable giving to ensure optimal tax savings.

THE NEW TAX LAW has changed the way that many Americans will complete their tax returns. The increase in the standard deduction ($24,000 for married couples and $12,000 for singles), combined with the elimination of many itemized deductions, will likely result in a 75% decrease in those who are able to benefit from itemized deductions.

Taxpayers who fall into this scenario are left with no tax benefit for charitable giving. However, there are two notable charitable giving strategies that could still save you money.

Bundling Your Gifts Using a Donor Advised Fund

A Donor Advised Fund is an investment account in which you:

1) Make an irrevocable contribution

2) Immediately receive the maximum tax deduction allowed by the IRS for your contribution

3) Request and direct grants to qualified charities of your choice in later years.

Here's an example. Sally and Fred donate $10,000 a year to charity. Prior to 2018, they've itemized their deductions and received a tax benefit on every dollar of giving.

Now, with the elimination of most itemized deductions, Sally and Fred are left with $10,000 of state and local tax deductions (the maximum allowed), plus the $10,000 of donations. This comes up $4,000 short of the new $24,000 standard deduction.

Instead of donating $10,000 each year without receiving additional tax benefit, Sally and Fred can lump multiple years of charitable giving into 2018, by putting the money into a Donor Advised Fund (DAF). If Sally and Fred lump five years of giving into 2018, they now have $60,000 of itemized deductions. In the 37% tax bracket, this is a tax savings of about $13,000. In each of the following four years, Sally and Fred will still receive the standard deduction of $24,000.

Sally and Fred still can distribute their donations at a rate of $10,000 a year to their desired charities from the Donor Advised Fund, while also providing the opportunity for tax-free growth on the remaining DAF assets.

Gifting From Your Retirement Account

Individuals over age 70 ½ can make up to $100,000 of charitable donations per year, directly from their IRA. This is referred to as a Qualified Charitable Distribution.

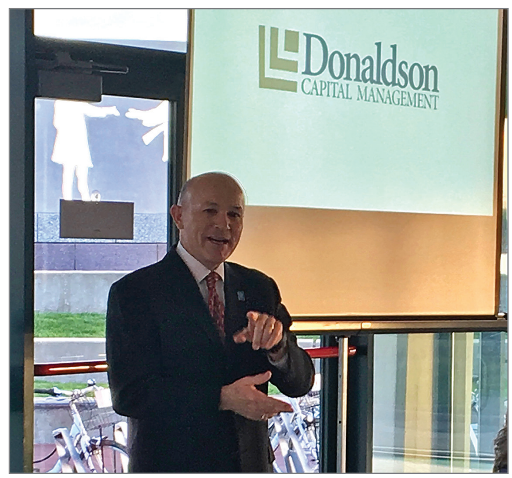
These distributions are tax free for federal and state and qualify to meet the individual's Required Minimum Distribution, which starts at age 70 ½. Facilitating these charitable distributions can be as easy as adding the checkbook feature to your IRA and writing checks directly to the charity.

It's important to remember that everyone's financial situation is different. What works well for Sally and Fred may not be the right strategy for you. We are here to help you figure out the most opportune strategy for your situation.

Vanderburgh County Medical Society Spring Mixer

Promoting Market and Financial Health in the Community

IN APRIL, DCM had the pleasure of hosting the annual Spring Mixer for the Vanderburgh County Medical Society. The Vanderburgh County Medical Society promotes the art and science of medicine and the betterment of public health. Kyle Markle, our Chief Investment Officer, had the opportunity to speak to the attendees about tax savings strategies and DCM's current market outlook. Thank you to the Vanderburgh County Medical Society and its members for all you contribute to your communities.



Randy Alsman, Sr. Portfolio Manager

Kyle Markle, Chief Investment Officer and Sr. Portfolio Manager

7 to 1: The Bull Market Continues, Part II

"How long can this bull market last?"

Eight indicators flashed warnings as the end of the 2000 and 2007 bull markets approached. Only one of those warnings is present today. Barring any shocks to the U.S. economy, the current bull market should continue.

IN EARLY 2016, we argued that the bull market would continue into 2017. 2016 would give investors plenty of worries:

- **Oil plunged to $26 a barrel in February. Many worried that Energy companies would default on loans and strain the entire financial system.**
- **The U.S. dollar became stronger.**
- **S&P 500 earnings declined every quarter.**
- **Following the UK's vote in June to leave the European Union, the Dow dropped 611 points.**
- **Then, a wild U.S. presidential election caused tremendous uncertainty in the markets.**

At the time of our 2016 letter, stocks had gone 91 months without a "bear market" (a 20% or more decline in prices). As this bull market looked to become the longest in history, financial reporters galore predicted its end. In 2016, we argued against relying on the length of past bull markets to predict future declines:

> **"If one had relied on average bull market duration to predict the demise of the 1990-2000 bull market, they would have been nearly five years early and missed out on almost 200% of returns." (7 to 1: The Bull Market Continues, October 2016)**

The stock market isn't on a timer. The length of time between bull and bear markets has no power to predict the future. So, what can?

Clients and friends ask us every day, "When is this bull market going to end?" Let's see if we can find any signs that today's bull is on its last legs.

As the bear markets began in 2000 and 2007, eight indicators flashed warnings. The future may not look like the past, but at least a few factors should be present at the next market top.

The following chart shows indicators and whether or not they are present today. A green "No" is a good thing — indicating that the event was not present in the market. A red "Yes" is a bad thing.

Event	2000	2007	2016	2018
Extreme valuations	Yes	No	No	No
Speculative buying	Yes	Yes	No	No
Increase in M&A and IPO activity	Yes	Yes	No	No
Rising interest rates	Yes	Yes	No	Yes
Weakening earnings	Yes	Yes	Yes	No
Eroding market breadth	Yes	Yes	No	No
Defensive sectors leading	Yes	Yes	No	No
Widening credit spreads	Yes	Yes	No	No

Following is an explanation of each indicator.

1. Extreme valuations - No

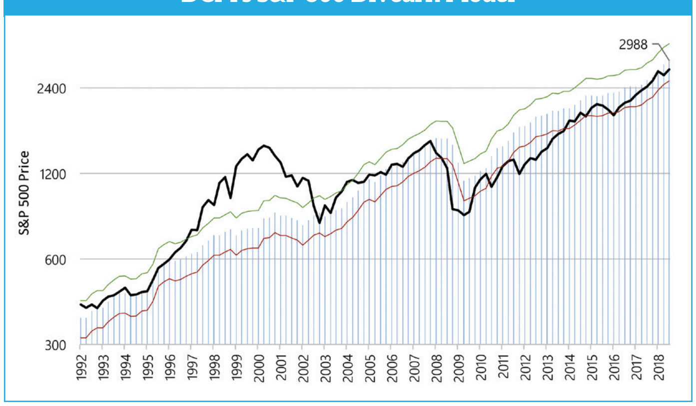
Financial commentators have been calling the market "overvalued" since 2013. They argue that the price-to-earnings (or "P/E") ratio has been running higher than average.

So what? The market's P/E means nothing by itself. A P/E of 20 could be expensive or cheap. It depends on interest rates and inflation. When rates and inflation are high, P/E ratios should be lower. In low-interest rate and inflation environments, P/E ratios should be higher.

Our valuation models consider these factors. Our "Divearn" model uses a blend of inflation, interest rates, dividends, and earnings. Since 1972, it has predicted roughly 95% of the long-term movement of the S&P 500.

What is that model saying today? Divearn predicts the S&P 500 should be trading around 2,970 today. That is roughly 9% higher than its current level. If 2018 earnings and dividends

DCM's S&P 500 Divearn Model



come in as expected, the model predicts the S&P 500 should reach 3,225 by year end. That's 18% higher by year end.

Even without a regression model, it's hard to argue today's market is expensive. The current P/E for the S&P 500, using the next 12 months' earnings, is 16.3. Over the past 20 years, forward P/E ratios have averaged 16.4. **Regardless of how you look at it, the market is not overvalued.**

2. Speculative buying - No

Market risk increases when exuberant investors pour money into stocks and push prices far above fair value. This happened in the late 1990s. Technology stocks attracted more money than their earnings justified and fueled a stock market bubble that eventually burst.

That optimism is not present in today's market. In April, investors pulled out $50 billion from equity mutual funds and Exchange-Traded Funds (ETFs). Some individual stocks are attracting speculative money (namely Facebook, Amazon, and Google). For the market as a whole, however, **we do not see broad-based speculative buying.**

3. An increase in IPOs - No

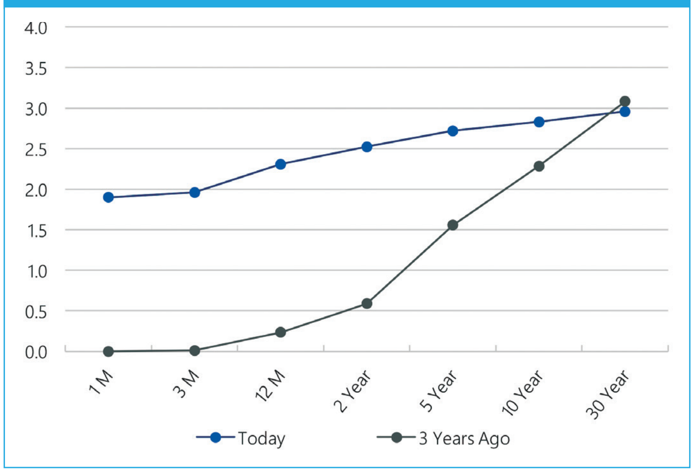
When a company decides to "go public," it sells shares via an Initial Public Offering, an IPO. Of course, the best time to take a private company public is when you can get the most money for it. During market tops, we should see a surge of IPOs. We don't see that today. **IPO activity is less than half of where it was in 2000 and well below its peak in 2007.**

4. Rising interest rates - Yes

High interest rates make bonds more attractive than stocks. Leading up to the 2000-2001 bear market, the 10-year U.S. Treasury bond yield increased from below 8% to more than 14%. From 2003-2007, Treasury yields rose from 3.5% to more than 5%. Since September 2017, short-term interest rates have doubled to more than 2.5% while 10-year U.S. Treasury yields have increased by more than 0.80%. Despite these increases, interest rates remain at historically low levels. They have yet to become a significant headwind for stocks.

Short-term interest rates have moved up faster than long-term rates, which has "flattened" the yield curve.

U.S. Treasury Yield Curve (Today vs. 3 Years Ago)



An "inverted" yield curve occurs when short-term rates are higher than long-term rates. An inverted yield curve has historically been a good predictor of recessions. The curve is not inverted, but it is closer than it was last year. The yield curve is something to watch but does not pose an imminent threat to stocks or the economy.

Add in the flattening yield curve, and the interest rate picture as a whole creates a **modest negative for stocks.**

5. Weakening earnings - No

U.S. tax reform and global economic strength have led to impressive growth in corporations' revenues and earnings. Q1 earnings for the S&P 500 companies grew by 20% over Q1 2017. Analysts project Q2 will increase by another 24.7%.[1] The strength in earnings growth has led to meaningful dividend increases. During the first five months of 2018, S&P 500 dividends grew 13.85%. That's the fastest pace of dividend growth since 2014.[2]

In our 2016 Bull Market Checklist, declining earnings was the lone "Yes" in our checklist. **Earnings (and dividends) now are a definite positive for stocks.**

6. Eroding market breadth - No

In healthy markets, price growth is widespread across many different stocks and sectors. It's not good for the market as a whole if just a few stocks and sectors are pulling the entire market. When many of the stocks are moving higher at the same time, we call that market "breadth."

So far in 2018, we've seen a few sectors and stocks perform particularly well. However, **we see broad participation from many stocks of varying sizes in all corners of the economy**. That is a sign both the economy and the stock market remain healthy.

7. Defensive sectors leading - No

In troubled times, investors shift towards quality, stability, and yield. A good indicator of market direction is how economically sensitive sectors are doing versus more defensive sectors. For example, utility companies typically do better than others in bad markets.

With the volatility we have experienced so far in 2018, you might expect defensive sectors to be doing well. However, offense has been defense in this market. In other words, the best performers have been the cyclical, growth-oriented sectors. So far in 2018, the only sectors to outperform the S&P 500 are the Consumer Discretionary (10.8%), Technology (10.2%), and Energy (5.3%) sectors. The worst performing are the defensive Telecom (-10.8%) and Consumer Staples (-9.9%) sectors.[3] **Cyclical sectors continuing to outperform is a good sign for stocks as a whole.**

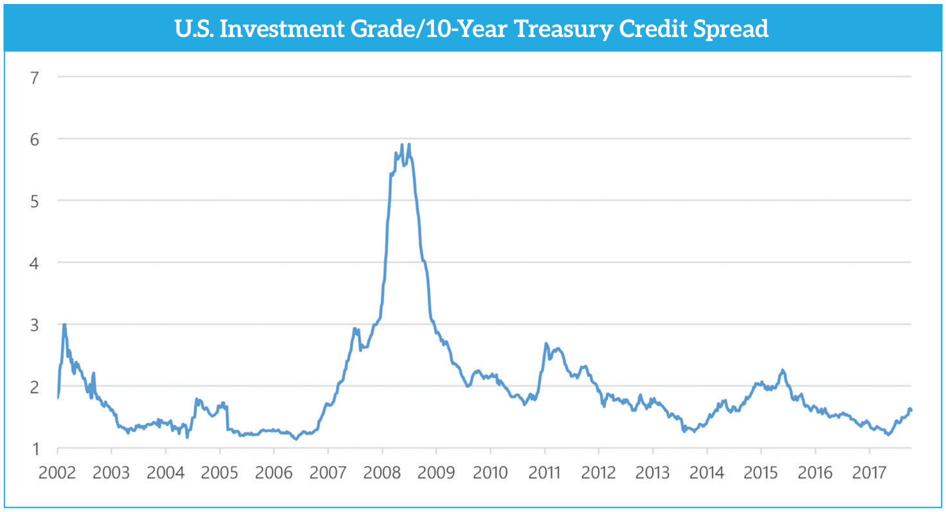
8. Widening credit spreads - No

As trouble looms in the economy, investors tend to sell riskier corporate bonds and move to U.S. Treasuries for safety. A "credit spread" is the difference between the interest rates on corporate bonds and the interest rate on U.S. Treasury notes. An increasing spread means investors believe corporate bonds are getting riskier.

From 2004 to 2007, credit spreads were narrow. However, those spreads widened in 2007 as the economy began to weaken. The same thing occurred in 2000 when the tech bubble came crashing down. **Today's credit spreads are wider than at the beginning of the year but are still close to all-time low levels,**[4] a good sign for both the economy and stocks.

Conclusion

Out of the eight indicators that pointed to a top in stock prices during 2000 and 2007, only one exists today. That said, we expect to see more volatility over the next few months.



Headlines continue to be negative. Talk of trade wars, "peak" earnings growth, and further Fed tightening continue to weigh on markets. November's midterm elections also will create uncertainty for investors. Stocks historically have been choppy in the months leading up to these elections.

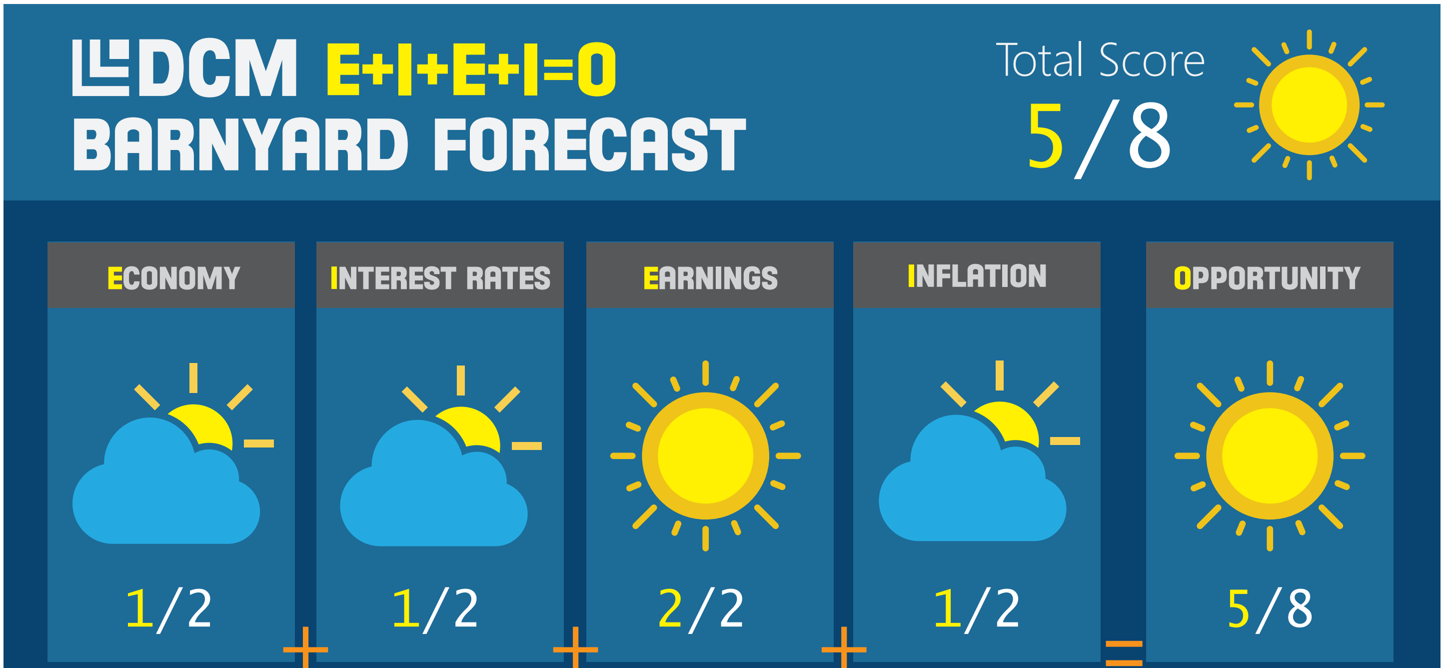
While volatility may remain, we still are optimistic. The underlying economic and business fundamentals are stronger than they've been in years. Until that changes, the bull market lives on.

1. S&P 500 trailing 12-month earnings per share at 6/30/2017 ($116.13) vs. 6/29/2018 ($131.22). Source: Bloomberg

2. 2014 dividend growth was 17.5%. Source: CNBC, "As companies sweeten dividend payouts, this is what investors need to know." June 5, 2018.

3. Source: Yardeni, June 29, 2018

4. As measured by the spread between the 10-year U.S. Corp BBB/Baa - 10-year U.S. Treasury spread (CSI BBB). Source: Bloomberg



This forecast provides DCM's evaluation of the overall economic climate. It is subjective in nature and represents the Firm's outlook and interpretation of the market as of the date of this publication. Each category is rated between 0 and 2 (0 being negative, 1 neutral, and 2 positive) and the cumulative score is measured as the opportunity. A total score between 0 and 2 indicates a negative outlook, 3 and 5 a neutral outlook, and 6 and 8 a positive outlook.

EMPLOYEE HIGHLIGHT

Zachary Chavira Earns AIF® Designation

AS A PART OF DCM'S NEW DIVISION, Retirement Plan Services (RPS), we added a new member to our team who brings expertise in the 401(k) industry. Zach Chavira joined DCM in August of 2017 as the Institutional Services Relationship Manager. Not only has he already added tremendous value to our 401(k) plans and participants, we also are pleased to announce he has earned his Accredited Investment Fiduciary® (AIF®) Designation.

The AIF® Designation has given Zach invaluable training and insight into the Fiduciary requirements that coincide with DCM's 401(k) services. We are now better equipped to serve our Plan Sponsors' and participants' best interest, while continuing to alleviate Plan Sponsors from much of the Fiduciary responsibility that a 401(k) plan requires.

Before joining DCM, Zach was a Financial Advisor in Henderson, Kentucky. He quickly obtained his Series 7, Series 65, Series 63, and Life Insurance Licenses.

Zach loves supporting local businesses and is a member of the Rotary Club. As an avid golfer and boater, he loves the opportunity to spend time with family and friends.

DCM Recognition

WITH MORE THAN 14,000 Registered Investment Advisors in the U.S., DCM has been named to the 2018 edition of the **Financial Times 300 Top Registered Investment Advisors** in the U.S. This is the fourth time that DCM has been recognized on this list.

FT FINANCIAL TIMES | Top Financial Advisers 2018

The Financial Times 300 Top Registered Investment Advisers is an independent listing produced annually by the Financial Times, an international daily newspaper (June 2018). The FT 300 is based on data gathered from RIA firms, regulatory disclosures, and the FT's research. The listing reflected each practice's performance in six primary areas: assets under management, asset growth, compliance record, years in existence, credentials, and online accessibility. This award does not evaluate the quality of services provided to clients and is not indicative of the practice's future performance. Neither the RIA firms nor their employees pay a fee to The Financial Times in exchange for inclusion in the FT 300.

Dow Jones — S&P 500 — NASDAQ

What do they all mean?

IT SEEMS EVERY DAY on the news you hear "... and today, the Dow Jones gained XX points, while the S&P was up only YY." What are these stock market indices, and what do they mean for your investments?

A stock market index is nothing more than a basket of stocks. The reports we hear each day tell us how much the combined prices of those stocks went up or down. Which stocks are selected and how the measurement is computed is specific to each individual index.

Dow Jones Industrial Average

First published by Charles Dow in 1896 and the most popular of the stock indices, the Dow Jones contains **only 30** large companies, like Disney, Home Depot, Exxon, and McDonald's. Nonetheless, with just 30 components, the Dow does less than the S&P 500 Index to represent the entire economy. The Dow is calculated on a price-weighted basis which gives companies with a higher share price a larger weighting in the index.

S&P 500

A committee at S&P Global carefully selects the 500 companies in this index in such a way that they closely mirror the U.S. economy. Calculations for the S&P include the size of each company, making it an excellent proxy for tracking the overall U.S. stock market. This also is why you might see DCM use the S&P 500 as a comparison to your portfolio's performance.

NASDAQ

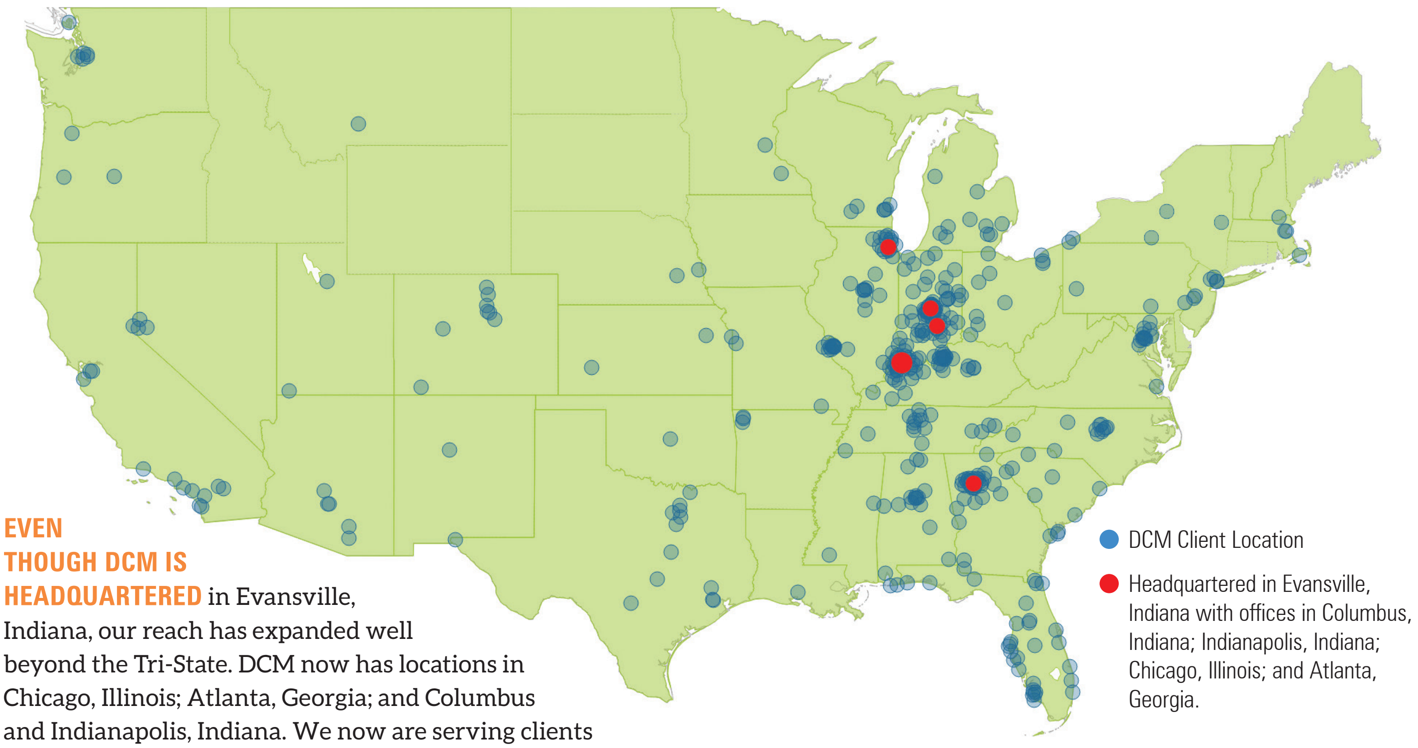
The Nasdaq Composite tracks approximately 4,000 stocks, all of which are traded on the Nasdaq exchange. The members of this index are heavily weighted towards information technology companies, making this a good index to follow if you're interested in the performance of the Technology Sector. Similar to the Dow, the Nasdaq is not the best representation of the overall market.

Of course, we **do not** recommend you become an "index watcher." Day-to-day changes in these indices mean very little when it comes to the bigger picture and the overall health of the U.S. economy. There might be good reasons for day-to-day fluctuations, but a focus on longer trends will inevitably be more rewarding.

Donaldson CAPITAL MANAGEMENT

Clients Across the Nation

Thanks to you, DCM now serves clients across 42 U.S. states



EVEN THOUGH DCM IS HEADQUARTERED in Evansville, Indiana, our reach has expanded well beyond the Tri-State. DCM now has locations in Chicago, Illinois; Atlanta, Georgia; and Columbus and Indianapolis, Indiana. We now are serving clients in 42 different states, as well as a handful of clients that reside outside of the U.S. In fact, only about a third of our clients live in southwestern Indiana. If you've not considered referring us to a family or friend in areas beyond our office locations, know that we are equipped and would be honored to serve any of your loved ones, regardless of where they may live.

POWER IN NUMBERS

New Additions to DCM will help maintain quality of service for you

THANKS TO YOU, DCM continues to grow. The primary source of our growth comes from friends you refer to DCM. So, we take very seriously our responsibility to have the right people and processes necessary to always maintain the quality of service that made you comfortable working with us and referring others.

Over the past four years, DCM has grown from 17 employees to 33. We have hired bright and capable people, keeping in mind while skills and procedures can be learned, values and attitude cannot. Therefore, we put a lot of time and effort into ensuring the people we hire meet Greg Donaldson's test of having "good heads and great hearts."

We also are investing in these folks via extensive training and education. And, they are investing in themselves. We have enough CPAs, CFPs, CFAs, CRPSs, FPQP's, and MBAs to confuse a pre-school teacher, and our staff still is studying.

Adding people has allowed us to specialize our talent so our Portfolio Managers can focus on what they love doing; serving you. Another benefit to specialization is we can develop experts in our other departments, like trading, research, and analysis. That allows PMs to deliver even better client service than was possible years ago when each PM had to juggle many other responsibilities.

Even though you may at times end up talking with someone here you hadn't previously met, we want you to know that when you become a client of DCM, the entire firm is at your service. Your resources are not limited to your Portfolio Manager and Client Services Manager. We put the tools and procedures in place to always make sure that your Portfolio Manager is aware each time you interact with anyone at DCM. We don't look at you as Ron Patberg's client, or Brandon Roop's client, or Beth Dietsch's client; we consider you a client of our entire firm, where there are 33 people eager every day to serve you.

Donaldson
CAPITAL MANAGEMENT

20 NW First Street, Fifth Floor ▪ Evansville, IN 47708 ▪ 800-321-7442 ▪ www.dcmol.com

INDEX DEFINITIONS S&P 500: Standard & Poor's (S&P) 500 Index. The S&P 500 Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad U.S. economy through changes in the aggregate market value of 500 stocks representing all major industries.