Decatur Capital Management Inc.

Decatur View – Third Quarter 2023 Update

The third quarter was negative for equity markets with the S&P 500 losing -3.3% return for the quarter. This brings the year to date, through September 30th, to 13.7%.

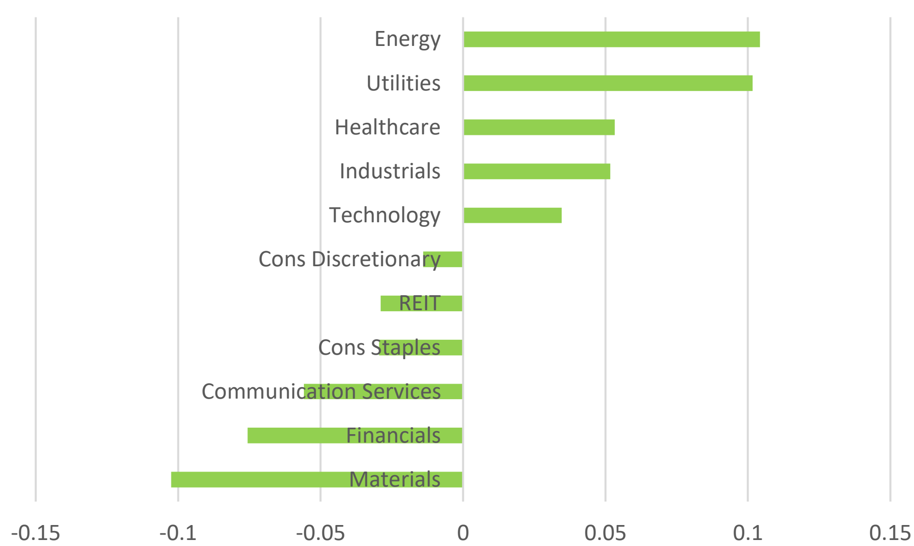
We have identified four drivers that are impacting markets in 2023. The drivers, in order of significance, are: 1) earnings expectations 2) the Federal Reserve controlling inflation, 3) continuing strain on banks, and 4) global threats.

Based on the four market drivers, we are cautiously optimistic on the capital markets.

Earnings Revisions

Chart 1 shows the average US net earnings revisions normalized, which provides a measure of market sentiment on the direction of earnings. The net analysts' revisions measure the number of analysts that are making positive changes to their earnings estimates compared to the number of analysts that are making negative changes to their estimates, scaled by the number of analysts. We normalized these values to measure the distance from the market net earnings revisions.

Chart 1: US 1 Year EPS Net Earnings Revisions Normalized, September 30, 2023



Source: Decatur Capital Management, Zacks Investment Research

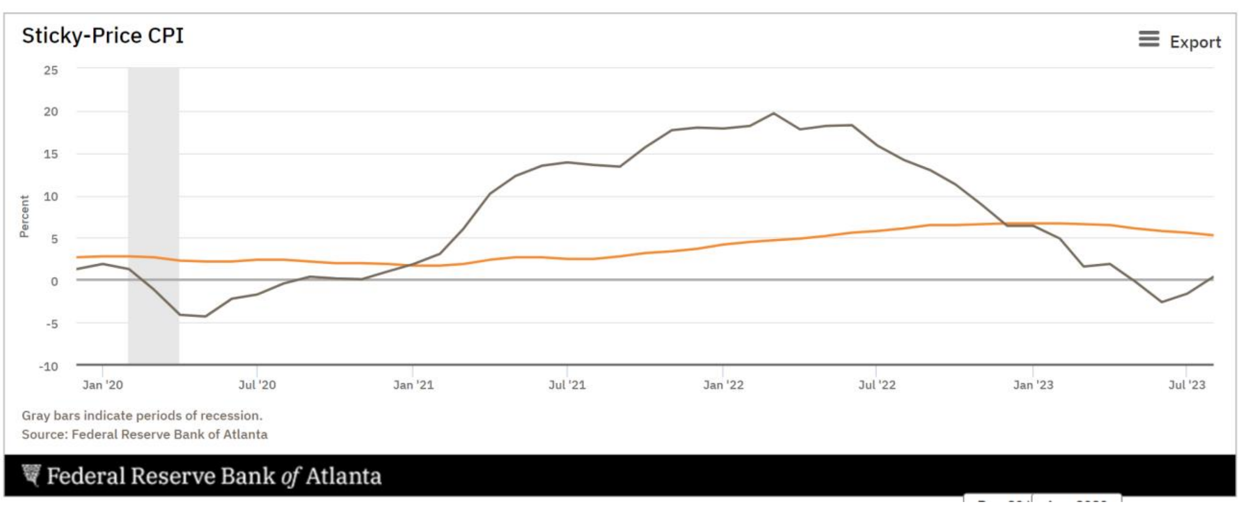
The outlook for the power sectors of energy and utilities is positively increasing. The utilities sector is coming off of a decade plus period of annual returns of approximately 11% and strong dividend growth. For 2023, utilities have returned -7%, significantly below the equity market returns. Currently, we are seeing that utilities are rebounding given their solid balance sheets, dividend yields, and current valuations. Energy earnings revisions continue to increase due to supply issues and growing demand. Also, healthcare continues to remain in the top five sectors for positive earnings revisions and will continue to perform well in this environment. Typically, healthcare is not an inflation sensitive sector since patients will continue to need pharmaceutical products. Also, analysts continue to increase their earnings estimates for the technology sector led by mega cap firms.

We continue to see lowering of revisions within financials and materials. We will address financials later in the report. Materials' outlook is declining with alternative energy, such as lithium, declining significantly in 2023. A mounting headwind for fertilizers / chemicals is that food prices are declining, which impacts farmers' ability to reinvest in fertilizers.

The Federal Reserve and Inflation

Federal Reserve (Fed) will remain resolute in controlling inflation. Chart 2 shows the two aspects of inflation, the sticky and flexible consumer price index. The orange line represents the sticky CPI, which as the name implies, is hard to get rid of and sticks around, such as rents and medical care. The grey line represents the flexible CPI. The flexible CPI includes those costs that may rocket up as inflation builds but are more easily controlled by the Fed, such as hotel rooms costs, entertainment tickets and eating out.

Chart 2: Sticky and Flexible Price CPI 12 month Rolling



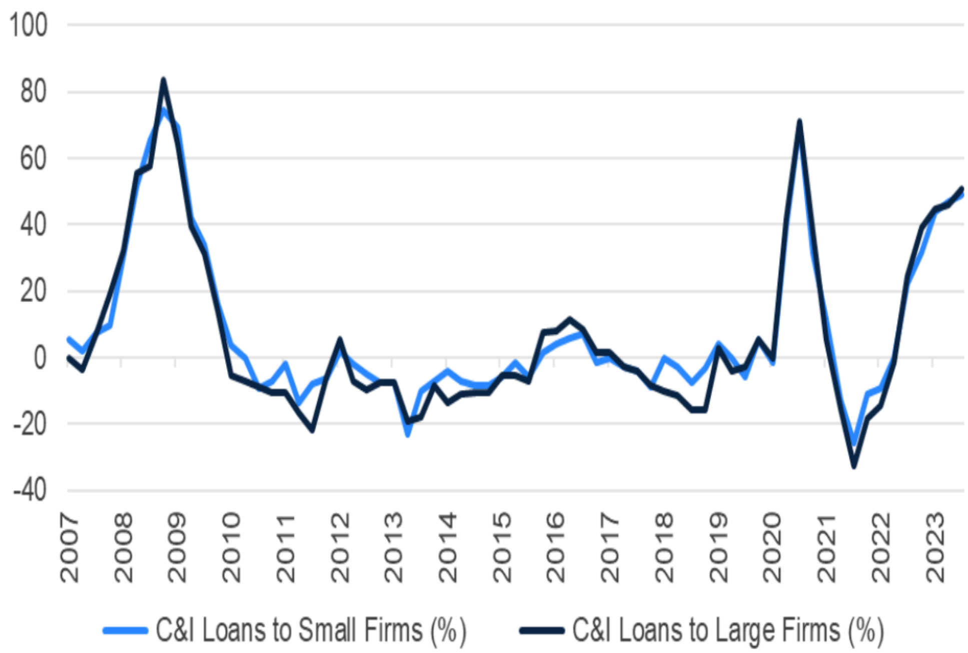
The Fed has paused increasing interest rates to evaluate the impact of earlier hikes on the economy. The sticky CPI, 5.3% has been trending downward while the flexible CPI increased slightly in July due to energy prices. Therefore, the recent pause in the hikes is reasonable as the Fed examines more data.

We believe that the majority of the Fed's rate hikes are behind us. The Israel – Hamas conflict may result in future pauses in the hike cycle since this is new data that needs to be evaluated. For our fixed income clients, we continue to employ maturity ladders that will benefit as yields increase with the Federal Reserve's future rate hikes.

Credit Contraction - Banks

The year of 2023 has been challenging for the banking industry. First there was the regional bank scare with a few banks closing. Now, we turn to commercial real estate and possible increasing loan delinquencies fueled by office buildings sitting vacant. Chart 3 shows the recent Fed's Senior Loan Officer Opinion Survey reported that lending standards tightened for commercial and industrial real estate loan categories to all borrowers.

Chart 3: Senior Loan Officer Opinion Survey

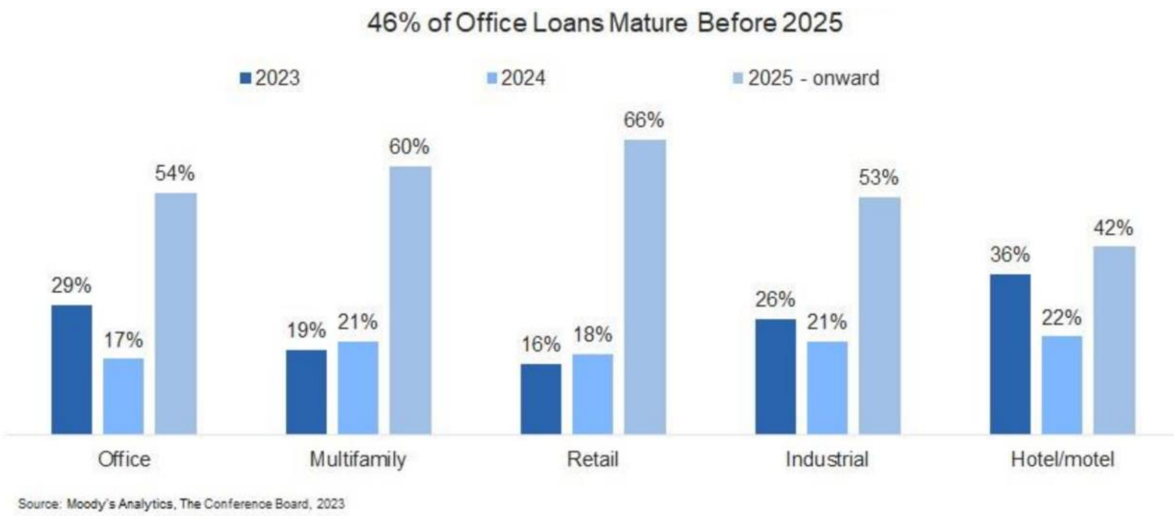


Sources: Office of Financial Research and The Conference Board.

We believe that banks' credit contraction is the canary in the coal mine and may indicate a further tightening of investments across the board. Chart 4 shows that approximately 34%

to 58% of real estate loans will need refinancing and at higher rates. The refinancing at higher interest rates could put additional pressure on companies.

Chart 4: Loan Maturities by Year & Property Type



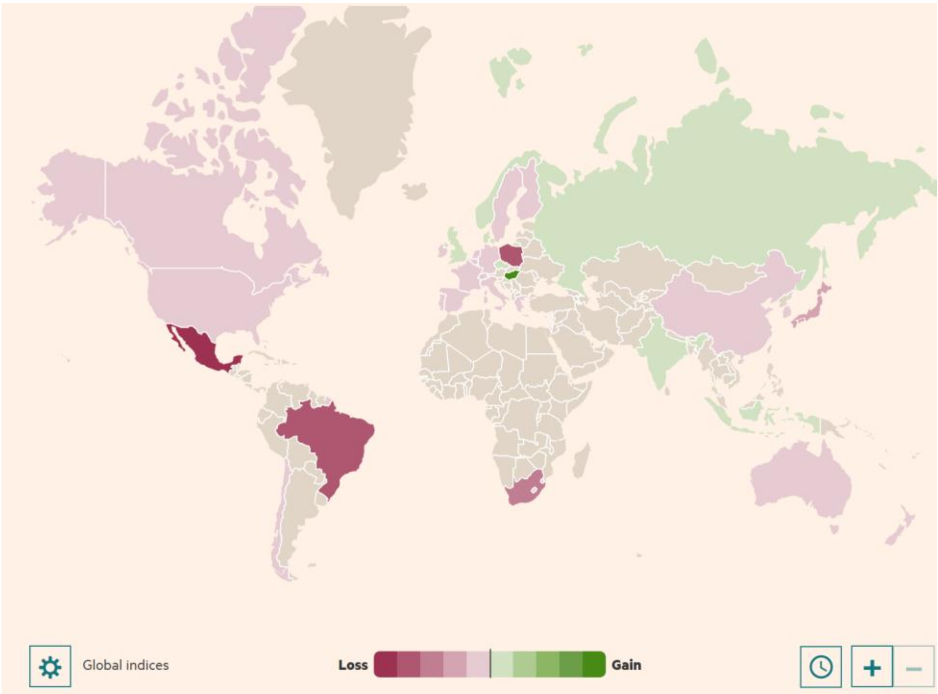
At the end of first quarter, we forecasted that the bank closures would not have a contagion effect on the rest of the banking industry. However, the negative market sentiment carried the regional banks down as a group. During second quarter, we reduced our overall exposure to regional banks. In the short term, our outlook for the banking industry is that earnings will be lower which may be a headwind for future price appreciation.

We continue to hold several banks in our quality dividend portfolio; however, we will underweight our exposure to banks for the remaining of the year and into 2024. We continue to believe that individual stock selection should provide better results than buying a broad regional bank fund.

Global Threats

At the beginning of the year, we were concerned with the Russia-Ukraine War and China's impact on global markets. The Russia-Ukraine War appears to be moving into a stalemate with no immediate resolution at hand. In addition, China and the U.S. have toned done the saber rattling.

Chart 5: Global 3rd Quarter Stock Return Map



https://markets.ft.com/data/world

Chart 5 shows the relative global performance during the quarter. As world economies fight inflation, most equity markets declined except for India and China. India is benefiting from manufacturing opportunities as companies search for alternate manufacturing facilities outside of China. Meanwhile, China introduced more than 50 economic support measures since May to increase investment into infrastructure projects and cutting taxes for businesses. In our All Country World excluding the U.S., we continue to overweight Latin America, Canada, and we are increasing our exposure to Asia.

Hamas' terrorist attack on Israel is an unexpected event. This continues to be a human tragedy and we believe that if the conflict remains within Israel's border that there will be limited impact to capital markets. We own one Israel based technology company and we will continue to monitor the situation.

Disciplined Approach

We realize that there could be risks that we simply cannot plan for. Conflict in the Middle East, such as the recent Hamas attack on Israel, is one such risk. We address these risks by staying true to our investment discipline. We continue to focus on companies that will survive catastrophic events based on the firms' leadership and competitive advantage. So, sticking to our mantra of profitability, expectations of stable or growing earnings, and valuation is how we manage these unknown risks.
