FLIPPIN, BRUCE & PORTER, INC.

INVESTMENT COUNSEL

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Most broad domestic equity indices posted mildly negative results for the first quarter of 2018 with the S&P 500 coming in at -0.8% and the Russell 1000 Value at -2.8%. It was the first time since 2015 that large-cap stocks fell during a calendar quarter. While the negative numbers for the period were relatively modest, that tells only part of the story. After a long hiatus, equity market volatility came roaring back during the first three months of the year. Stocks surged in January, with the year-to-date return for the S&P 500 peaking at more than 7.5% through the twenty-sixth of that month. From there, it took only nine trading days for those gains to be erased and for the S&P to slip into correction territory, down 10% from its previous high. Many investors were shaken by the decline, as it had been more than two years since the market had experienced any meaningful selloff. After stabilizing and recovering during much of February and March, another sharp decline near quarter end took the markets into red territory for the period. Approximately 37% of the market value gained by the S&P 500 since the presidential election in November 2016 was evaporated in the correction, according to calculations by financial firm Raymond James.

Wall Street pundits point to two main factors that triggered the negative sentiment shift for stocks: rising interest rates due to inflation worries and fears of an international trade war. These risks certainly bear monitoring. Jerome Powell's appointment as chairman of the Federal Reserve became effective during the quarter. New leadership adds an element of uncertainty regarding the magnitude and pace of forthcoming hikes to the fed funds rate expected for 2018. We believe the FOMC is likely to maintain its plan for three additional incremental increases this year. If so, we would expect gradual rate increases across the yield curve which should not cause significant disruptions to equity markets, especially considering the underlying strength of the economy. The bigger wild card is how White House trade policy will play out. Certainly, major disruptions to the global trading system would not be good for the U.S., China, Mexico or any other economy. Our hope is that the initial trade tariffs and the trade-related tweets by President Trump are meant to strengthen the U.S. position as negotiations continue.

We remain favorably disposed toward the equity markets even as volatility has increased. Falling stock prices and rising earnings expectations, primarily due to the tax cut enacted in December, have changed valuation calculations such that stocks are now more reasonably priced. S&P 500 earnings per share are estimated to grow almost 18% this year and another 8% in 2019, resulting in a price/earnings ratio of 17 times earnings for 2018 and 15.6 times for next year. Our portfolio offers even more attractive valuation, trading at roughly 13.5 times earnings. While it is difficult to predict short-term moves in the market, we believe the potential has improved for solid returns from these levels over the longer term.

The total return for our Large-Cap Value portfolio, while negative for the quarter, was significantly ahead of the Russell 1000 Value benchmark and in line with or slightly better than the S&P 500. Year-over-year results reached double-digit returns for the portfolio. Portfolio activity included increases in Devon Energy and CenturyLink and a new purchase of CBS Corp.

CBS is currently in talks to merge with Viacom, not unexpected given that the Redstone family has sizable positions in each company. We believe CBS's media assets are strong, which puts it in a slightly favorable position as negotiations progress.

Returns for our Equity & Dividend Plus portfolio were ahead of the Russell 1000 Value but behind the S&P 500. Longer-term returns remain favorable, especially compared to the value benchmark. Of note, the portfolio outperformed both indices during the correction phase of the quarter, demonstrating one of the positive attributes of the strategy. Another benefit of the strategy is its ability to generate consistent and growing cash flow through both dividends and call option premiums. That attribute is especially beneficial during low return environments like we have experienced so far this year. During the quarter, we made a new investment in Pepsico and increased our weightings in a number of other holdings. We reduced weightings in several other names through option activity.

For additional firm wide information please visit our website at www.fbpinc.com or call us at 1-800-851-3804. As always we appreciate your continued interest in our firm.