April 13, 2012

Dear Friends of Coho Partners:

What a difference six months makes. Back in the summer/early fall of 2011, our markets were mired in fear – fearful of a double-dip recession both here and abroad as economic statistics flagged, very concerned that the Eurozone was coming apart at the seams with local and potentially global repercussions and finally fixated on the embarrassing and potentially disruptive political brinksmanship here at home in the fight over the debt ceiling amid hints of potential civil unrest (Occupy Everything). The domestic economy has since picked up some real, if shallow, momentum with increases in employment measures, auto sales, consumer confidence, great weather (!) and even some signs our long housing nightmare might at least be stabilizing. Shallow, still, in that incomes have not kept pace with spending, confidence has only increased to levels typical of typical recessions and long term fiscal/structural imbalances that remain to be addressed, perhaps after the next election. And we at Coho remain very concerned that the long range costs incurred in terms of deficits and distorted economic behaviors for this welcome, if shallow boost, have been enormous and most likely, still to be realized.

The stock market, compared to this continued tepid recovery, however, is soaring. Maybe with hindsight the Fall lows of 2011 were discounting way too much gloom or maybe investors now see a much stronger economy looking forward, but either way the market is up 26% since the end of September and pretty much in a straight line. The underlying tone has changed as well. While 2011 ended with modestly positive returns, a peek under the hood revealed something more akin to a stealth bear market as less cyclical, lower beta, higher quality issues clearly outperformed the rest, as the market hunkered down in the midst of everything mentioned in the prior paragraph. The Coho portfolio benefited handsomely from that market on a relative basis. This observed cautiousness changed dramatically, however with the turn of the new year, as all that lagged in 2011 has soared in 2012 (with the exception of Apple, which just soars period) and the "risk-on" trade dominated. Please note the table printed below highlighting the absolute performance of economic, quality and beta sectors of the market for both 2011 and the first quarter of 2012. The differences in behavior of defensive characteristics (defensive sectors, higher quality, lower beta) vs. more aggressive ones (cyclical sectors, lower quality, higher beta) were quite significant in calendar 2011 vs. q1 2012. What worked in 2011 was a considerable laggard in q1 2012, and vice verse.

Absolute Returns:

Economic Sectors	**2011**	**Q1 2012**
Utilities	19.7	-1.7
Cons Staples	14.0	5.5
Health Care	12.7	9.0
Telecomm Services	6.3	2.1
Energy	4.7	3.9
Cons Discretionary	6.0	16.0
Technology	2.4	21.5
S&P	**2.1**	**12.6**
Industrials	-0.7	11.3
Materials	-10.0	11.1
Financials	-17.1	22.1

S&P Quality Ranking	**2011**	**Q1 2012**
A+	11.5	7.0
A	10.8	7.7
S&P	**2.1**	**12.6**
A-	-1.4	13.6
B+	2.4	13.3
B	0.1	17.7
B-	-24.3	22.2
C	-28.0	21.4
NR	5.6	11.6

Beta Quintiles	**2011**	**Q1 2012**
Beta 1 (low)	13.2	4.1
Beta 2	11.4	11.0
S&P	**2.1**	**12.6**
Beta 3	0.8	17.4
Beta 4	-6.1	17.6
Beta 5 (high)	-16.7	20.0
NA	6.7	14.1

Source: Thomson Reuters, Baseline, Coho Partners.

If you have been a regular investor/follower/student of Coho Partners, you would not be surprised at all by where our investment preferences lie. Our first priority at Coho is to protect portfolios in difficult times – and as such, our portfolios are always tilted toward the defensive. In the table below, note the average weights in the Coho portfolio in the more defensive areas of the market vs. that of the S&P. Each area – sectors, quality and beta are arranged in order of defensiveness (roughly so in the case of the sectors) and represent the average weight for each category over the 2011-1q 2012 period. Note how our portfolio weights are tilted heavily toward the top of each category, especially versus the S&P. This is very typical for Coho. Less cyclical, higher quality, lower beta stocks with defensive business models are a constant. Thus our portfolios benefitted to such a large degree last year when the markets were so defensive (risk-off). Conversely, when market weights *and preferences* are tilted so heavily in the opposite direction, like this past quarter (risk-on), this makes for our most difficult periods of relative performance and on this we did not disappoint. One of the nicer distinctions of our pattern of returns, however, is that while times such as this past quarter are our most difficult relative periods, they are also typically very attractive periods on an absolute basis as well, and hopefully we did not disappoint terribly here, either.

Average portfolio weights, 12/31/2010 - 03/31/2012:

Economic Sectors	**% of portfolio**		
	Coho	**S&P**	**Diff**
Cash	3.6	0	3.6
Utilities	0.0	3.5	-3.5
Cons Staples	30.4	10.9	19.6
Health Care	18.0	11.5	6.6
Telecomm Services	0.0	3.0	-3.0
Energy	12.2	12.4	-0.3
Cons Discretionary	10.3	10.7	-0.4
Technology	12.0	19.0	-7.0
Industrials	9.8	10.9	-1.1
Materials	0.1	3.6	-3.5
Financials	3.7	14.7	-11.1

S&P Quality Ranking	**% of portfolio**		
	Coho	**S&P**	**Diff**
Cash	3.6	0	3.6
A+	46.4	20.7	25.7
A	20.6	7.2	13.4
A-	3.3	15.3	-12.1
B+	14.8	23.7	-8.9
B	3.1	17.4	-14.4
B-	0.0	5.3	-5.3
C	0.0	0.5	-0.5
NR	4.1	7.8	-3.7
NA	4.3	2.0	2.3

Beta Quintiles	**% of portfolio**		
	Coho	**S&P**	**Diff**
Cash	3.6	0	3.6
Beta 1 (low)	35.7	27.1	8.6
Beta 2	34.4	18.4	16.0
Beta 3	23.0	22.2	0.8
Beta 4	3.4	18.4	-15.0
Beta 5 (high)	0.0	12.7	-12.7
NA	0.0	1.3	-1.3

Source: Thomson Reuters, Baseline, Coho Partners

Now the last two years have started off very similarly, only to face a difficult next few quarters and then ultimately rally strongly at the end of each respective year. It is very tempting and not without real merit to think the same pattern might occur again. The economy is still unnaturally propped up by a combination of incredible Fed stimulus and fiscal spending which (hopefully) has nowhere to go but down from here. It is also troubling that consumer real incomes and job growth cannot get going simultaneously. Congress remains completely dysfunctional and the tone of the elections are unlikely to inspire a lot of confidence. Europe's problems have been temporarily masked by a flood of liquidity, but not remotely solved. China continues to slow and is starting to cast a pall across all emerging markets and some developed ones as well. Finally, the market has enjoyed a massive run accompanied by the aforementioned internal mood change to favoring risk. We may be perfectly ripe for the old adage of "sell in May and go away".

On the flip side, this just might be the start of the self sustaining, materially stronger economic recovery that we've all been hoping for - one that starts to reverse the drag of low consumer and business confidence, government deficits, high unemployment, etc. Worries abound, to be sure, but it is in such environments that good economies and bull markets are born. The US corporate sector is flush with cash, cash flow and balance sheet firepower that could be put to work when the time is ripe. The US consumer has gone a long way to repair his/her balance sheet and is exhibiting some signs of pent up demand. There is nothing quite as magical as an economy that starts to feed on itself and gets into the vortex of positive reinforcement. Growth begets growth which begets more growth and all recent nightmares are forgotten as seemingly intractable problems get "solved" when the economy grows faster than expected for a significant period of time. Fear gives way again to greed and all is well. We just may be on the cusp of such a pleasant economic surprise.

The nice thing about Coho's philosophy is that we don't need to know the ultimate outcome of the current debate. It won't change our investment philosophy either way. We constantly search for companies with less-than-market cyclicality, high quality balance sheets, transparent business models, strong free cash flow generation, long term sustainable growth equal to or slightly better than the market and good dividend growth. To that end we added a few new holdings to the portfolio this quarter in Air Products (APD), International Flavors and Fragrances (IFF) and Lowe's Companies (LOW). APD is a major player in the industrial gas segment, an industry with wonderful long term prospects in the developed economies and also a beneficiary of the industrialization of the emerging economies. Much of their business model is defined by long term take or pay contracts which help protect their profits in tough times. IFF can be viewed as a "connector company" to the diversified multinational, regional and local companies that differentiate their products based on taste or scent. We swapped out of our holding of Home Depot and into Lowe's, keeping some exposure to the improving do-it-yourself home improvement sector, but moving funds into the more attractive company at this time.

We hope that the pattern of the last two years of a summer slump does not repeat itself, but feel as prepared as ever if it does. In the meantime, enjoy the early Spring and the good markets.

Thank you for your continued trust and interest in Coho Partners.

Sincerely,

Peter A. Thompson	Brian L. Kramp, CFA
Partner / CIO	Partner / Portfolio Manager / Analyst