July 5, 2012

Dear Friends of Coho Partners:

June was a good month for domestic equities, but not good enough to offset the weakness from the prior two months. Some of the generous first quarter gains were lost but returns remain solidly positive for the year. During the more challenging second quarter backdrop, we were able to insulate the portfolio from a good portion of the retreat, and by doing so, have narrowed our first quarter underperformance during which the market posted a sizeable advance.

The volatility that investors are witnessing is likely to persist. As truly long term investors, we too are frustrated by this whipsaw action, but we do not control it nor can we avoid it. We prefer to remain focused on understanding the long term operating and financial strategies of our companies so that we can apply conservative assumptions to our five year dividend discount models in order to assess the relative attractiveness of our investable universe. This deliberate process has worked effectively in the past and we believe it will remain helpful in achieving our desired pattern of returns, which is strong relative performance during the down periods and competitive returns when the market advances.

We used the market's volatility to our advantage twice in June. We eliminated our long term holding in Family Dollar. When we first bought Family Dollar in 2007, few investors were appreciative of the value of "dollar" stores. More recently, dollar stores have become quite the rage and the valuations reflect this. Earlier this year we reduced this position as the stock price rose and the expected rate of return declined, but in June, the stock surged again and the expected rate of return fell to a level where we had to sell the remaining position. On the other hand, we established a new position in Nike, following a large sell off on supposedly disappointing fiscal fourth quarter earnings. We have owned this high quality company in the past and believe the decline in valuation was very much overdone and the longer term outlook remains quite strong. These are good examples of how our valuation discipline takes advantage of volatility.

There are concerns on many fronts, which suggest a conservative and defensive portfolio orientation is appropriate. On the domestic front, we still are dealing with persistently high unemployment, weak consumer confidence, the upcoming election, and uncertainty over tax rates in 2013. The recent Supreme Court ruling on the Affordable Care Act removed an uncertainty and now we will see how that decision impacts the healthcare sector.

Western Europe is struggling with its well publicized Eurozone problems, while China's economy slows. All of these trends suggest more tepid global GDP growth and thus a defensive investment orientation. At the present time, the portfolio has a generous dividend yield of 2.9% and a forward four quarter P/E of 13x, which is only slightly above the portfolio's long term expected earnings growth rate. The companies within the portfolio have business models that tend to do relatively well during periods of weak economic activity because they make products or provide services that people demand all the time. As such, there is a higher recurring revenue stream, which supports earnings growth, which in turn allows for annual dividend growth.

Regarding dividends, June was another good month, as United Health and Walgreens increased their dividend by over 30% and 22% respectively. As we begin the second half of the year, all but five of our holdings have increased their indicated rate for 2012 and we fully believe the remaining companies will follow suit as is their custom in the second half of this year. In an environment where returns are challenging, dividend income and possibly more importantly, the growth in that income, will go a long way towards cushioning downturns, while still playing an invaluable role in allowing for participation during advancing periods.

Second quarter earnings season will begin in earnest this month. We are optimistic that our holdings will deliver acceptable results against their long term operating and financial strategies. We will be reporting back to you on this progress in subsequent letters.

Sincerely,

Peter A. Thompson

Brian L. Kramp, CFA