OUR DIVIDEND GROWTH NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

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Valuentum Securities Inc.
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We'll be adding a new page 2 to the supplemental dividend reports that can be found on each stock's individual page on the website: www.valuentum.com. We'll be rolling them out with each new industry update!

Annualized Return	Annualized Goal	Outperformance
12.8%	Mid-High Single Digits	5.3pts

*Please see note below regarding performance measurement.

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"Monetary policy is a relative game, not an absolute one."
– Brian Nelson, CFA

***NOTE:** The Dividend Growth portfolio's goal is to generate a mid-to-high single digit annual return (about 7.5%) over rolling 3-5 year periods. As of today, February 1, 2016, the portfolio is significantly exceeding this goal.

Dividend Growth 'Bubble' To Continue But For How Long?

By Brian Nelson, CFA

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Best Dividend Growth Ideas:
MO, AAPL, CBRL COH, CSCO, XLE, GE, HAS, HCP, INTC, JNJ, MDT, MSFT, O, PG, PPL (TLN), VNQ

Latest Alerts, see page 4

New: Cracker Barrel (CBRL), *today*
New: Vanguard REIT ETF (VNQ), *today*

You've heard about low interest rates. You may have even heard about a ZIRP, zero interest-rate policy, as had been the case in the US for years, but have you heard of NIRP, negative interest-rate policy?

Well, that's the latest with respect to Japan (EWJ), which is home to the third-largest national economy in the world after the US and China. On January 29, the Bank of Japan (BOJ) introduced a negative benchmark interest rate of -0.1%, meaning that instead of paying interest on deposits, it will charge commercial banks to hold their money. This may make Japanese exports cheaper to stimulate growth, but my goodness, talk about a move to push "parked" assets out of the country. The US Treasury markets felt the accelerated asset flow (i.e. the "carry trade") Friday, helping to drive US government bond yields lower and US equities higher, despite news that the US economy grew less than 1% in the fourth quarter of 2015.

From where we stand, the move by the BOJ looks a lot like a "Hail Mary" pass to see if Japan can finally escape deflation and get economic growth back on track. The causes behind Japan's deflationary spiral are many and varied, but cheap labor across other emerging Asia nations coupled with pricing pressure from a competitive export market are at least two primary considerations, with some pointing to aging demographics as a contributing cause. Whatever the primary drivers behind Japan's sluggish growth, the BOJ's "Hail Mary" pass may fall incomplete, and we're viewing the odds as long that any monetary policy, by any one nation or collective group of countries, as in the ECB, will permanently solve all the world's economic ills. It simply can't. Monetary policy is a relative game, not an absolute one.

Japan is not the only major economy to have negative interest rates. The European Central Bank (ECB), which oversees the monetary policy of the European Union, the largest collective economy in the world, began paying -0.1% (negative 0.1%) on deposits in June 2014, and it has even lowered that rate since then, deeper into negative territory. Perhaps the ECB is the daring example that Japan has followed (Sweden, Denmark, and Switzerland also have negative interest rates). No matter the precedent, the US markets applauded the news from the BOJ, but we're not buying it fundamentally. The move, in our view, has merely augmented the artificial "carry trade," a favorite for

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*Dividend Growth Bubble...*from previous page

overleveraged hedge funds. For example, now hedge funds levered to the hilt can borrow yen even more cheaply to convert to an appreciating dollar on a Treasury bill (TLT, TBT) of a relatively higher-quality and higher-yielding rate. Yikes.

There are few things to take note of. First, the data points pointing to global deflation are adding up. We're certainly not advocates of speculating in the "yellow, shiny" metal (i.e. gold), but traders coming to the same conclusion will start to look to this widely-believed, global deflationary-hedge (GLD). Second, if we were to have any adverse shocks to the US-Japanese exchange rate, we could be in for quite a spill in the event this "carry trade" unwinds. In light of the summer blues of 2015 that generated worries of an emerging-market currency crisis, from Brazil to South Africa and beyond, the risks are certainly piling up. Third, it may be the case that the "surprise" move by Japan may have given the upward march in interest rates in the US pause, at least for the time being.

Fed chair Janet Yellen and team have been communicating to the broader financial markets that the US federal funds rate will go higher, with the next move speculated in March, but many are now betting following the move by the BOJ that the last hike was a policy error, meaning interest rate hikes could be on hold. Many have been positioning for rising interest rates, but could Japan's move be the catalyst for a change-of-opinion, further inflating dividend–paying stocks than offer higher income streams that US Treasury assets? From our perspective, the chances of a very low interest rate environment continuing for the foreseeable future have increased, which could push yield-seeking assets "back" into dividend-paying stocks, propelling the duration of the "dividend growth" bubble.

Equity investors have been flocking into the dividend-heavy consumer staples (XLP) sector, with the sector garnering nearly a 20 times earnings multiple on its collective earnings stream. This isn't a sector filled with high-flying technology stocks (XLK, TDIV) or biotech (IBB) "darlings," but we're talking about companies like Coca-Cola (KO), Wal-Mart (WMT), Altria (MO) and Procter & Gamble (PG), for instance. We hold the latter two in the Dividend Growth Newsletter portfolio, but please be careful with these high-yielding consumer brand names. Though more discretionary in nature, McDonald's (MCD), for example, is trading at 20 times fiscal 2017 expected earnings of $6 (which itself may be too optimistic), consumer staple Procter & Gamble is trading at 20 times fiscal 2017 expected earnings per share of $4 (amid a widespread brand transformation), while 3M (MMM) is trading at ~17 times fiscal 2017 expected earnings per share of $9 (perhaps a cyclical peak). Again, these measures are expected annual earnings tallied, not at the end of each firm's fiscal 2016, but at the end of fiscal 2017, which could very well approximate the peak of global economic growth for some time to come. We're more than 6 years removed from the March 2009 panic bottom.

Of course we're not jumping ship early (a classic shortcoming of a pure "value" process), but we are walking a tight-rope as we let these "types" of dividend-paying equities with "lofty" forward earnings multiples run in the Dividend Growth Newsletter portfolio for the sake of income. A 10%-15% correction may not be worth it for some income investors, and they have to think hard about whether receiving a 3%-5% yield is worth experiencing some capital erosion. What we fear the most is that it is very possible that investors are "falling in love" with the brand names, business models and dividend checks of these widely-known equities, forgetting that valuation will always be the supreme magnet that drives all share prices over the intermediate- to long-term. The size of the yield should never be the only consideration within any investment framework. Just look at what happened to investors in Seadrill (SDRL) or Teekay LNG (TGP) or Kinder Morgan (KMI), for example.

As it stands now, 2016 may turn into the year where the "bubble" in organic dividend paying stocks really inflates following the bursting of the "bubble" of financially-engineered distributions of MLPs in 2015. Please be sure to catch up with, "5 More Reasons Why We (Had Expected) Kinder Morgan Shares to Collapse" (they did). There's a great image in that write-up that walks through how "bubbles" inflate within equities that have financially-engineered payouts, or ones not paid out of free cash flow, as measured by cash flow from operations less all capital spending, and/or earnings.

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*Dividend Growth Bubble...*from previous page

In any case, many feel that "recession-resistant, safe-haven" consumer-staple entities may be the place to hide and get paid to do so in 2016, and they may be right. Just look at top-weighting Altria (see page 5), for example – shares have now surged past $61 each!

We're not going to take our eye off the fundamental risks, but we're watching developments closely to not get caught up in the bust. Hope you enjoy this February edition of the Dividend Growth Newsletter!

Johnson & Johnson Reports Strong Underlying Performance

By Kris Rosemann

As US-based multinational corporations continue to battle currency headwinds related to the strong US dollar, Johnson & Johnson (JNJ) reported solid underlying results in its most recent quarter and full-year report, released January 26.

Johnson & Johnson reported full-year sales in 2015 of $70.1 billion, which represents a 5.7% decrease on a reported basis from 2014 due to a negative currency headwind of 7.5 percentage points. On an operational basis, sales grew 1.8%, domestic sales advanced 2.6%, international sales grew 1.1% on an operational basis, and sales excluding acquisitions, divestitures, and hepatitis C sales on an operational basis increased 6.5% on a year-over year basis.

The underlying growth witnessed in 2015 at Johnson & Johnson was driven by its 'Pharmaceutical' business and a variety of its iconic 'Consumer' brands. The Consumer business advanced sales by 2.7% on an operational basis from 2014, with international sales growth being slightly higher than domestic sales growth in constant currency. The segment accounted for ~19% of total revenue in the year. Over-the-counter products such as Tylenol and Motrin, upper respiratory products such as Zyrtec allergy medication, and digestive health products were positive contributors for the segment, as were international feminine protection products, Listerine oral care products, and Neutrogena skin care products.

Johnson & Johnson's 'Pharmaceutical' business was its best performing segment in 2015, as it grew sales 4.2% on an operational basis. Domestic sales outpaced international sales on a constant currency basis, and the segment made up nearly 45% of total revenue. The strong performance in this segment was driven by both the strength of existing core products and higher growth in new products. We're not surprised by either of these drivers, as we have long been high on the pharmaceutical pipeline of the company.

Growth in the segment was partially offset by lower sales of the firm's hepatitis C offerings, which continue to face significant pressure from competitive entrants as sales fell nearly 70% on an operational basis from 2014. We would expect this headwind to continue in the near term as more competing offerings are expected to enter the market in 2016. However, the company did acquire Novira Therapeutics, a privately-held clinical-stage biopharmaceutical company that develops innovative therapies for curative treatment of chronic hepatitis B, which has the potential to expand its portfolio to other strains of the hepatitis virus.

Key drivers of sales growth for Johnson & Johnson's 'Pharmaceutical' business were new products, including its type 2 diabetes treatment, its once-daily blood cancer therapy, its oral anticoagulant, a once-daily medication for the treatment of metastatic and castration-resistant prostate cancer. Also providing growth were some of its more established products including its psoriasis and psoriatic arthritis treatment, an injectable schizophrenia treatment for adults, an ADHD treatment, and a treatment of a number of immune-mediated inflammatory diseases. While the growth rates in these products may not have been as high as some of the new products, but the continued strength in their performance provided a strong base for the segment's revenue in 2015.

In 2015, Johnson & Johnson delivered on its expectation to continue the strength of its 3 core brands that had each already delivered more than $1 billion in revenue, as well as achieving the same feat with 7 new products that were targeting the $1 billion in individual revenue mark.

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As we said after the third quarter of 2015, the firm has as strong a pipeline as ever, and it continued its momentum in relation to new approvals from the FDA and new regulatory submissions for the expansion of existing products to new treatments and new products in the fourth quarter of the year. The company will continue to invest in 12 key new products that are planned to be filed for approval by 2019, each of which has the potential to reach the $1 billion in annual revenue mark.

Johnson & Johnson's 'Medical Devices' was the firm's weak link in 2015, as sales fell 1.4% on an operational basis from 2014. Domestic sales grew by 1% in the year, while international sales fell by 1.7% on an operational basis. The segment accounted for ~36% of total revenue in 2015, and the company recently announced a restructuring plan for the segment. The restructuring initiative is expected to save $0.8-$1 billion in pre-tax costs annually by 2018, $200 million of which is expected to be realized in 2016, while targeting the acceleration of its pace of innovation and improving its go-to-market model.

The restructuring of the 'Medical Devices' business will result in the segment cutting 4%-6% of its global workforce over the next two years. The business will be reported in the following divisions moving forward: Cardiovascular; Diabetes; Diagnostics; Orthopedics: Hips, Knees, Trauma, Spine & Other; Surgery: Advanced, General, Specialty; and Vision Care. $2-$2.4 billion in restructuring charges will be incurred by 2017 in relation to the move, $600 million of which was recorded in the fourth quarter of 2015.

The true highlight of the fourth quarter of 2015 for Johnson & Johnson was the tremendous jump in its diluted earnings per share of more than 29%, to $1.15. Adjusted diluted earnings per share, which excludes the restructuring charge related to the Medical Devices business and after-tax intangible amortization expense, advanced 5.1% to $1.44. This shows the decrease in special items and expenses from the fourth quarter of 2014 to the fourth quarter of 2015, and we think the adjusted growth number of approximately 5% is the more 'representative' number for earnings growth for the year.

Looking ahead to 2016, Johnson & Johnson is expecting modest top-line growth on an operational basis similar to that of 2015 of 2.5%-3.5%. Adjusted earnings per share are expected to be in a range of $6.43-$6.58, representing growth of 5.3%-7.7% on an operational basis from 2015. Currency headwinds are expected to continue to drag on results in the near term, but organic performance looks solid. We will be following management's plans to restructure its 'Medical Devices' business closely, while its 'Consumer' business continues to provide a steady revenue stream, but the clear driver behind the firm's operations going forward remains its Pharmaceutical business. Johnson & Johnson continues to be a core holding in the Dividend Growth Newsletter portfolio.

Alerts: A Long-Time Favorite from the Bullpen and An Interest Rate Risk Hedge

By Brian Nelson, CFA

We've long appreciated the stand-out dividend strength characteristics of Cracker Barrel (CBRL) among the full-service restaurant space, and we see an opportunity to add the company to the Dividend Growth Newsletter portfolio today (see page 5). We've outlined our case for Cracker Barrel in the past, "Free Cash Flow Feeds Cracker Barrel's Dividend Growth," and while we haven't quite gotten our price just yet, we're going to inch forward a bit with a small 1.5% position in the Dividend Growth Newsletter portfolio at this time. The company yields a very nice ~3.4%, and its Dividend Cushion is solid for that high of a payout.

One of the areas we're expecting Cracker Barrel to surprise to the upside is the positive impact from vacationers taking to the roads thanks to plummeting gas prices. Not only are falling prices at the pump a stimulant for road trips, but we think Cracker Barrel may be most to benefit from this trend, given that its restaurants can often be found very close to exits off the interstate or next to lodging and accommodations. The company truly has a differentiated concept, in our view, and it generates as much as 20% of revenue from its retail store business. The cash keeps coming in even as would-be diners wait for a seat. It has an excellent business model, and Cracker Barrel makes it work well. We're adding 18 shares at $133.50 each.

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The Dividend Growth Portfolio

Annualized Return	Annualized Goal	Outperformance
12.8%	Mid-High Single Digits	5.3pts

DIVIDEND GROWTH PORTFOLIO -- as of February 1, 2016 (intraday) — Dividend Growth Portfolio Inception Date: January 1, 2012

Company Name	First Purchase	Avg Cost ($)	# of Shares	Total Cost ($)	Last	Current Value ($)	% of Portfolio	Exp. Yrly Div's ($)
Altria (MO)	12/30/2011	29.65	101	3,001.65	60.86	6,146.86	3.8%	228.26
Apple (AAPL)	7/24/2013	63.17	51	3,228.45	95.97	4,894.47	3.0%	106.08
Cisco (CSCO)	11/14/2014	26.15	100	2,622.00	23.28	2,328.00	1.4%	84.00
Coach (COH)	9/19/2014	37.55	80	3,011.00	36.79	2,943.20	1.8%	108.00
NEW: Cracker Barrel (CBRL)	**2/1/2016**	133.50	18	2,410.00	133.50	2,403.00	**1.5%**	79.20
Energy Sector SPDR (XLE)	4/1/2015	72.63	121	8,795.76	56.50	6,836.50	4.2%	262.33
General Electric (GE)	10/21/2013	26.18	240	6,290.20	28.66	6,878.40	4.2%	220.80
Hasbro (HAS)	12/30/2011	31.89	110	3,514.90	73.00	8,030.00	4.9%	202.40
HCP (HCP)	9/19/2014	40.11	75	3,015.25	36.22	2,716.50	1.7%	172.50
Intel (INTC)	12/30/2011	24.25	289	7,015.25	30.80	8,901.20	5.4%	300.56
Johnson & Johnson (JNJ)	12/30/2011	65.58	107	7,024.06	103.54	11,078.78	6.8%	321.00
Medtronic (MDT)	12/30/2011	38.25	157	6,012.25	76.20	11,963.40	7.3%	238.64
Microsoft (MSFT)	12/30/2011	25.96	154	4,004.84	54.72	8,426.88	5.1%	221.76
Proctor & Gamble (PG)	12/30/2011	66.71	105	7,011.55	81.15	8,520.75	5.2%	278.25
PP&L (PPL)	12/30/2011	29.42	238	7,008.96	35.96	8,558.48	5.2%	359.38
Realty Income (O)	7/24/2013	44.35	60	2,668.00	56.90	3,414.00	2.1%	142.80
Talen Energy (TLN)	6/1/2015	Spin off	29	Spin off	6.84	198.36	0.1%	NA
NEW: Vanguard REIT ETF (VNQ)	**2/1/2016**	77.07	32	2,473.24	77.07	2,466.24	**1.5%**	140.54
Latest changes: Cracker Barrel and Vanguard REIT ETF were added today, February 1.								
Cash -- changes in monthly cash balance reflects dividends received and trading				2,363.42		57,062.24	34.8%	3,466.50
Dividend Growth Portfolio				100,000.00		**163,767.26**	100.0%	**TBD**
DG Portfolio Annualized Return (from inception through current date)								**12.8%**
DG Portfolio Annualized Return Goal (Mid-to-High Single Digit Returns)								7.5%
DG Portfolio Annualized Return Outperformance								**5.3%**
SPDR S&P Dividend ETF (SDY)								**10.6%**

UR = Under Review

** Upper bound of fair value range noted.

***** The yield an investor would have received if they had held the fund over the last 12 months assuming the most recent NAV.

This portfolio is not a real money portfolio. Data as of February 1, 2016 (intraday). Cost basis includes commissions. Results include divdends, but no interest received on cash balance.

DIVIDEND GROWTH PORTFOLIO -- as of February 1, 2016 (intraday) — Fundamental data as of February 1, 2016

Company Name	Yrly Div's Paid ($) / Shr	Div Yield %	Ex Div Date	Next Pay Date (cycl)	Div Cushion™	Div Safety	Div Growth	Fair Value	VBI Score	Price/Fair Value
Altria (MO)	2.26	3.71%	mid-Mar 2016	mid Mar 2016 (quart)	1.2	GOOD	GOOD	$55.00	6	1.11
Apple (AAPL)	2.08	2.17%	early Feb 2016	Feb 2016 (quart)	5.3	EXCELLENT	EXCELLENT	$142.00	3	0.68
Cisco (CSCO)	0.84	3.61%	early Apr 2016	early Apr 2016 (quart)	3.2	EXCELLENT	EXCELLENT	$37.00	9	0.63
Coach (COH)	1.35	3.67%	early Mar 2016	early Mar 2016 (quart)	2.0	GOOD	EXCELLENT	$38.00	6	0.97
NEW: Cracker Barrel (CBRL)	4.40	3.30%	mid Apr 2016	late Apr 2016 (quart)	1.3	GOOD	GOOD	$132.00	4	1.01
Energy Sector SPDR (XLE)	2.17	3.84%	late Mar 2016	early Mar 2016 (quart)	-	GOOD	NEUTRAL	-	UR	-
General Electric (GE)	0.92	3.21%	early Mar 2016	Mar 2016 (quart)	2.1	GOOD	GOOD	$31.00	6	0.92
Hasbro (HAS)	1.84	2.52%	late Apr 2016	mid May 2016 (quart)	1.9	GOOD	GOOD	$71.00	6	1.03
HCP (HCP)	2.30	6.35%	early Feb 2016	early Feb 2016 (quart)	1.3	GOOD	GOOD	$46.00	3	0.79
Intel (INTC)	1.04	3.38%	early Feb 2016	early Mar 2016 (quart)	2.5	GOOD	GOOD	$38.00	9	0.81
Johnson & Johnson (JNJ)	3.00	2.90%	late Feb 2016	early Mar 2016 (quart)	2.4	GOOD	EXCELLENT	$111.00	6	0.93
Medtronic (MDT)	1.52	1.99%	late Mar 2016	Mar 2016 (quart)	1.6	GOOD	EXCELLENT	$67.00	4	1.14
Microsoft (MSFT)	1.44	2.63%	mid Feb 2016	mid Mar 2016 (quart)	2.6	GOOD	EXCELLENT	$55.00	6	0.99
Proctor & Gamble (PG)	2.65	3.27%	late Apr 2016	early May 2016 (quart)	1.5	GOOD	EXCELLENT	$67.00	7	1.21
PP&L (PPL)	1.51	4.20%	early Mar 2016	early Mar 2016 (quart)	Held for diversification reasons.			$28.00	6	1.28
Realty Income (O)	2.38	4.18%	monthly	monthly	1.5	GOOD	GOOD	$55.00	6	1.03
Talen Energy (TLN)	NA	NA	NA	NA	-	-	-	-	-	-
NEW: Vanguard REIT ETF (VNQ)	4.39	5.70%	late Mar 2016	early Apr 2016 (quart)	-	GOOD	NEUTRAL	-	UR	-

Standard Disclaimer: Our Dividend Growth portfolio is for information purposes only and should not be considered a solicitation to buy or sell any security. Valuentum is not responsible for any errors or omissions or for results obtained from the use of our Dividend Growth Newsletter and accepts no liability for how readers may choose to utilize the content.

*Alerts...*from page 4

We're also taking a stab at the lowest cost exposure to the REIT industry in the form of the Vanguard REIT ETF (VNQ). The Bank of Japan's decision to pursue negative interest rates has put pressure on government bond yields in the US, with many are now speculating that the Fed will pause with respect to contractionary monetary policy. We've been mighty pleased with the addition of Realty Income (O) to the Dividend Growth Newsletter portfolio and even embattled HCP (HCP) has managed to bounce back toward cost. With the energy MLP space (AMLP) in shambles, we think high-yield seekers may be more prone to accepting REIT-related risk in an interest rate environment that no longer looks decidedly upward for the foreseeable future. We're adding 32 shares of the Vanguard REIT ETF at $77.07 each to capture such a view.

The Vanguard REIT ETF's top holdings include Simon Property Group (SPG), Public Storage (PSA), Equity Residential (EQR), AvalonBay Communities (AVB), and Welltower (HCN). Annualizing the Vanguard REIT ETF's latest quarterly distribution of $1.10 per share translates into a ~5.7% dividend yield at current prices. Our ETF work on the real estate industry can be found at the following link, and we've highlighted the Vanguard offering as one of our favorites:

http://www.valuentum.com/articles/20150319

Methodologically speaking, the US equity markets have punished stocks almost indiscriminately. At times, we may stretch the Valuentum Buying Index criteria (which has started to pick up the market's weakening technicals) to gain incremental exposure to preferred sectors/industries, as that with respect to the REITs in this instance. We generally remain quite firm with respect to the Dividend Cushion ratio, however. The higher the Dividend Cushion ratio, the more resilient the payout, and negative Dividend Cushion ratios should be cause for concern in a tightening credit market.

P&G Puts on Impressive Display of Pricing Strength

By Kris Rosemann

Multinational corporations have seen reported revenue punished in recent quarters as a result of the strong US dollar relative to other currencies around the world. In keeping with this theme, Procter & Gamble (PG) reported net sales falling 9% in its fiscal second quarter of 2016 on a year-over-year basis to $16.9 billion. However, after backing out all the noise, the company's constant-currency core earnings per share leapt more than 20% on a year-over-year basis in the period. Reported free cash flow trends were fantastic through the first half of the fiscal year, too, and while we think the company's valuation remains stretched, we're not rushing to remove it from the Dividend Growth Newsletter portfolio anytime soon.

The real "story" of the P&G quarter lies in the firm's ability to continue its pricing strength across all five of its reporting segments, which has led a return to companywide organic sales growth. Pricing had a positive impact of 3 percentage points on total net sales in the quarter, led by an impressive 6 percentage point jump in its 'Grooming' segment, while organic sales in aggregate advanced 2% in the quarter, flat or higher in all five reporting segments from the year-ago period. Volume growth in every segment, however, was lower (down 2% organically), with 'Beauty' products volume dropping 7% led by weakness in its Olay brand. Though the large drop in volume across the board was rather concerning, we were very pleased with the company's pricing performance, which could offer material upside for the rest of fiscal 2016.

P&G's 'Grooming' and 'Health Care' segments led the charge with both achieving 3% organic sales growth in the fiscal second quarter. Though volume in the 'Grooming' segment shrank 2% in the period, the division benefitted from significantly higher pricing in shave care, and innovative growth in its Braun brand in developed markets more than offset lower volume in the remainder of the segment. The 'Grooming' segment also reported the highest pricing benefit of any of the firm's segments with a 6% benefit in the quarter. Constant-currency net earnings in the 'Grooming' segment, however, faced some headwinds (down 5%) due in part to mix, and we'll be watching closely to see if there may be something else going on that's not easily adding up.

Please see *Procter & Gamble...*on next page

***Procter & Gamble…*from previous page**

The 'Health Care' segment, on the other hand, was boosted by a favorable geographic mix and sales growth in Oral Care in developed markets and Personal Health Care in developing markets. The segment received a 3% benefit on its top line from pricing and mix, while losing 3% from organic volume. Unlike the 'Grooming' segment, however, where constant-currency net earnings fell, the 'Health Care' segment turned in robust constant-currency net earnings growth of 20% in the quarter on a year-over-year basis.

Procter & Gamble's 'Fabric Care and Home Care' segment grew organic sales by 2% from the year-ago period, and it was the weakest of the five divisions in terms of pricing strength in the quarter, as it only received a 1% top-line benefit from pricing. Both 'Fabric and Home Care' performed well in developed markets, but this growth was partially offset by 'Fabric and Home Care' declining in developing markets. The segment turned in the highest constant currency net earnings growth in the quarter with a 26% jump from the same period in fiscal 2015 thanks to a material decline in commodity costs associated with the division. Organic sales in Procter & Gamble's 'Beauty' segment grew a mere 1% in the quarter, as a 4% positive impact from pricing was offset by lower volume. Poor performance from the Olay brand partially offset gains from one of the segment's super-premium skin care brands. The 'Beauty' division advanced its constant-currency net earnings 9% on a year-over-year basis; currency headwinds remain a major issue for reported results in the segment.

Volume was also an issue for the 'Baby, Feminine, and Family Care' segment, where organic sales remained unchanged from the year-ago period. The division's organic sales declined as growth in its Pampers brand in the US was offset by declines in other regions, and Family Care organic sales were unchanged despite increasing in North America as well, while Feminine Care organic sales increased thanks to innovation in developed markets and pricing strength in developing markets. Currency headwinds have had a strong impact on this segment as well, as net earnings fell 10% in the quarter but grew 5% on a constant currency basis when compared to the year-ago period.

Procter & Gamble's pricing strength added to a strong quarter for earnings. Gross margin jumped 170 basis points in the quarter thanks to pricing gains but also due to lower commodity (input) costs. SG&A expenses declined 180 basis points as a percentage of revenue in the quarter thanks to overhead spending reductions in-line with its productivity efforts and lower restructuring and other charges. These improvements led to operating profit margin increasing 340 basis points versus the fiscal second quarter of 2015. P&G's core earnings per share grew 9% on a year-over-year basis to $1.04, and when excluding the impact from currency exchange rates, core earnings per share leapt 20%+ in the quarter. Through the first half of the fiscal year (ending December 31), free cash flow surged thanks to stronger cash-flow-from-operations generation ($8 billion versus $7.1 billion) and lower capital spending ($1.2 billion versus $1.6 billion). The firm continues to repurchase shares at a high rate, spending $2 billion on buybacks in the most recent quarter, though we think the dividend is a better use of its cash.

As we look to the rest of fiscal 2016, Procter & Gamble is maintaining its expectation for organic sales growth to be in-line to up low-single digits from fiscal 2015, while "all-in" sales are expected to be down high-single digits on the year due to currency headwinds, minor divestitures, and deconsolidation in Venezuela. Major top-line growth should not be expected anytime soon from the company. The company projects core earnings per share to be down 3%-8% compared to fiscal 2015's $3.76 core earnings per share, but on a currency-neutral basis, core earnings-per-share is expected to increase at a mid-to-high single digit rate pace for fiscal 2016. P&G also changed its adjusted free cash flow productivity to 100% (was 90%) of adjusted net earnings for the full fiscal year after a strong quarter of free cash flow generation.

Procter & Gamble's pricing strength and productivity initiatives offered a material boost to margins and currency-neutral core earnings per share in the quarter, and the growth in a variety of the firm's brands in developed markets thanks to innovation initiatives showed that the decision to reconfigure its portfolio holds merit. We'll also be paying attention to its new 'limited home laundry pickup initiative, and whether that gains any meaningful traction. That said, however, volume pressures across the board are hard to overlook, and management still has a long way to go to successfully transition the portfolio for the long term; significant currency headwinds certainly are not helping the situation. Shares are trading at 20+ times fiscal 2016 constant-currency core earnings per share, as the firm retains a $17 billion net debt position. We're maintaining our high-$60's fair value estimate at this time.

Apple Will Go Lower… And It Will Be "Forced" Into Acquisitions

By Brian Nelson, CFA

We have a few regrets for not "lightening up" more on the position in Apple (AAPL) in the newsletter portfolios during the past few weeks, "Looking to Trim Apple…" and while our lack of action may cost the newsletter portfolios a few basis points in the near term, we're not too concerned. For one, in this "type" of market, we want to stick with quality, and Apple fits that bill quite well, particularly with the cushion that its balance sheet provides. The iPhone giant's equity price may go lower as some sell the "headlines" around its fiscal 2016 performance, but the company's financial health puts it in a class by itself, in our view.

The *Journal* hit the wires with some pretty nasty headlines, noting that "Apple said iPhone sales grew at the slowest pace since its introduction in 2007 and forecast that revenue in the current quarter will decline at the steepest rate in 15 years…" Quarterly revenue missed consensus expectations by more than $700 million, with sales of iPhones, iPads, and Macs all coming in below expectations in the quarter. Reported operating income and cash flow from operations also dropped from the year-ago period. Apple issued fiscal second-quarter revenue guidance of $50-$53 billion, below a consensus mark of $55.6 billion. If this weren't enough to disappoint, the executive team said it has started to see "some signs of economic softness" in China. We don't think the quarter and outlook could have been set up any worse for the stock.

That said, we still think Apple will be a relative outperformer in a weak equity market, something that we're expecting during 2016. Though a disappointment relative to expectations it was, Apple's quarter still witnessed record revenue of $75.9 billion, record income of $18.4 billion, and an impressive gross margin, up from the year-ago period. Despite coming in lower than expectations, Apple also delivered "all-time record sales of iPhone, Apple Watch and Apple TV" in the period, as it noted that the growth of its Services businesses accelerated. These were all good things, but the question -- "is this quarter the peak?" – will in our opinion continue to weigh on shares. Fundamentally, we're most concerned that reported operating income barely budged from last year's period, perhaps the greatest indication that a performance "ceiling" has been hit. Free cash flow generation in the period also waned considerably.

As we expect shares to inevitably face some weakness in coming months, we would expect pressures to continue to mount on what CEO Tim Cook and the executive team should do with its considerable cash balance, which on a net basis, reached $160 billion at the end of the quarter ($215.7 billion gross). Buying back stock isn't offering much "bang for the buck" in light of the paltry multiple on earnings-per-share numbers, and while ongoing increases in the dividend will be nice, the yield will serve mostly to act as support for the equity, in our view, not as a catalyst for new heights, at least in the near term. Repatriating the cash to the US in order to foot a large tax bill simply isn't going to happen, and why should it? Apple generates more than two thirds of its business overseas anyway.

On the basis of our valuation process, Apple is not getting sufficient credit for its large cash balance. As a result, we would expect the executive team, if pressured by a weak stock price, to eventually be "forced" into some deal-making to translate such cash into an earnings stream, most likely by picking up a non-US target such that earnings growth can be had and US taxes can be circumvented. We think M&A will become of considerable more importance to the Apple "story" in 2016, far more than it has ever been in the past.

Recent news that has stated Apple is unhappy with its car progress may make California-based Tesla (TSLA) a take-out candidate (~$25 billion market capitalization), but it's more likely a foreign car maker with forward-looking technology may fit the bill as Apple will seek to put its foreign reserves to work tax-free, should it go in that direction. Apple will likely not bother with a GoPro (GPRO) or a Pandora (P), nor do we think a deal with undervalued Qualcomm (QCOM) is likely, even if it is possible, but scooping up non-US-based entities in its supply chain does make a lot of sense, in our opinion. Apple has ~60 percentage points of margin (1 less the gross margin) it could effectively "buy" in coming years

Please see *Apple…*on next page

*Apple…*from previous page

to grow earnings and pave the way for higher returns.

As share pressures mount and Apple gets even less credit for its overseas cash balance, look for the company to start shopping around, if it hasn't already started to build a list of takeout candidates. There may be nothing more straightforward than vertical integration and cutting costs from the system to bolster returns, and the market may soon "force" it to start making such deals. CEO Tim Cook will be tested in 2016, and the executive team will soon have to start sorting good targets from bad. Carl Icahn may also make a return visit.

A large deal could already be in the works…we wouldn't be surprised.

General Electric's Results Remain "Messy"

By Brian Nelson, CFA

There's something to be said about a company that can handle just about anything thrown at it.

Since the founding of the Dow Jones Industrial Average (DIA) just before the turn of the 20th century, the composition of the 30 stock index has changed more than 50 times. There's one company, however, that has retained its relevance in the broad market benchmark the longest. That company is General Electric (GE), which has been a staple of the DJIA since 1907, well over a century now. For long-term investors, there's no better example of a company that has handled just about every market cycle than the industrial giant.

In recent years, General Electric has been working to shake off the stigma related to "overextended" financials exposure attained during much of the "Jack-Welch" era, a move that came back to haunt the company during the Financial Crisis of 2008-2009, which forced the conglomerate to cut its dividend. Some income investors felt betrayed in light of the move to slash the payout and may never come back to shares (no matter what), but we think the "new" General Electric has learned from its recent "troubled" past. From where we stand, its future is bright, even after considering some of challenges exposed during fourth-quarter results, released January 22.

For starters, we continue to applaud the executive team's refocus on its high-return, defensible industrial operations, now expected to account for 90% of earnings by 2018 (was 58% in 2014). The spinoff of Synchrony Financial (SYF) and its Retail Finance businesses were nice steps toward de-risking its consolidated portfolio, and management noted that it has divested $150+ billion in financials assets thus far, paving the way for "de-designation" as a SIFI, or "systematically important financial institution" (i.e. too big to fail). Not only will ditching nearly all of its financials exposure remove financial "contagion" risk, thereby reducing its cost of capital (project hurdle rates), and a hefty regulatory burden, but it will also increase flexibility to drive better returns across the remainder of its portfolio. The "GE Capital exit plan" is expected to be largely complete by the end of 2016.

Still, portfolio acquisitions from Alstom's Power & Grid business to Halliburton's (HAL) drilling assets and pending portfolio divestitures including its 'Appliance' business to China's Qingdao Haier will continue to "muddy" GE's proforma financials, but we did like the company's target it released in December for 2016 "operating earnings" to rise to $1.45-$1.55 per share, up from its 2015 per-share of $1.31 number in 2015, to be propelled by as much as a 15% expected jump in operating income. GE remains on track to return more than $90 billion to investors from 2015 to 2018 and is targeting a return of ~$26 billion to shareholders in 2016 (~$8 billion dividend; $18 billion buyback), down from ~$33 billion in 2015 but still a very robust figure. The company reaffirmed these targets when its released fourth-quarter results.

That said, GE's fourth-quarter 2015 results could have been a lot better, and we're growing less and less comfortable with the presentation of its financials. Industrial segment organic revenue dropped modestly on a year-over-year basis in the quarter as its 'Renewable Energy' and 'Oil & Gas' segments weighed on performance, but its 'Healthcare' segment and its soon-to-be-divested 'Appliances' division also contributed to the decline. GE's 'Power,' 'Energy Management,' 'Aviation,' and 'Transportation'

Please see *General Electric's Results…*on page 13

Stocks with High Valuentum Buying Index Ratings and Strong Dividend Growth Prospects

By Valuentum Analysts

The table below showcases firms in our coverage universe that have high Valuentum Buying Index™ ratings and strong dividend growth prospects. The table represents a list of interesting dividend-paying stocks that are *among* the most timely dividend growth ideas based on our stock-selection methodology. You'll see that many of them are already holdings in our Dividend Growth portfolio (see page 5).

Though our dividend-growth portfolio is near fully-invested, we may swap in firms on this list or firms on our dividend-growth watch list (see the next page) at the right price or if our analyst team determines that a new add has more potential total return opportunity than a current holding. At any time, however, our favorite dividend growth ideas are included in the Dividend Growth portfolio.

Company Name	Symbol	Sector	Div Yield	VBI	Div Growth	Div Cushion
Omega Healthcare	OHI	Financials	6.5%	6	EXCELLENT	2.0
Iron Mountain	IRM	Industrials	6.1%	6	GOOD	1.6
Universal Health Realty	UHT	Financials	5.3%	6	GOOD	1.5
Quality Systems	QSII	Health Care	4.9%	7	GOOD	2.0
Realty Income Corp	O	Financials	4.8%	6	EXCELLENT	1.5
Hewlett-Packard	HPQ	Information Technology	4.3%	6	GOOD	2.7
Altria Group	MO	Consumer Staples	4.3%	6	GOOD	1.2
Brookfield Infrastructure	BIP	Energy	4.3%	6	GOOD	1.2
Coach	COH	Consumer Discretionary	4.3%	6	EXCELLENT	2.0
Guess	GES	Consumer Discretionary	4.1%	6	EXCELLENT	2.4
ABB	ABB	Industrials	4.1%	6	GOOD	1.6
QUALCOMM	QCOM	Information Technology	3.8%	6	EXCELLENT	3.7
Superior	SUP	Consumer Discretionary	3.7%	6	GOOD	2.0
Abercrombie & Fitch	ANF	Consumer Discretionary	3.6%	6	GOOD	2.7
NTT Docomo	DCM	Telecom Services	3.5%	6	GOOD	1.9
Reynolds American	RAI	Consumer Staples	3.4%	6	GOOD	1.4
Procter & Gamble	PG	Consumer Staples	3.4%	7	EXCELLENT	1.5
Paychex	PAYX	Information Technology	3.3%	6	EXCELLENT	2.6
Enbridge	ENB	Energy	3.3%	6	EXCELLENT	2.3
Intel	INTC	Information Technology	3.3%	9	GOOD	2.5
Western Union	WU	Information Technology	3.2%	7	EXCELLENT	2.8
Darden Restaurants	DRI	Consumer Discretionary	3.2%	6	GOOD	1.7
Unilever PLC	UL	Consumer Staples	3.1%	6	GOOD	1.5
Diebold	DBD	Industrials	3.1%	6	GOOD	1.9
Compass Minerals	CMP	Materials	3.1%	6	GOOD	0.8
Waste Management	WM	Industrials	3.1%	6	GOOD	1.6
General Electric	GE	Industrials	3.1%	6	GOOD	2.1
Unilever N.V.	UN	Consumer Staples	3.1%	6	GOOD	1.5
Cisco	CSCO	Information Technology	3.0%	9	EXCELLENT	3.2
United Parcel Service	UPS	Industrials	3.0%	7	EXCELLENT	1.8

At any time, our favorite dividend growth ideas are included in the Dividend Growth portfolio, page 5.

The Dividend Growth Watch List

By Valuentum Analysts

The dividend growth watch list, which is proprietary to the Dividend Growth Newsletter, showcases firms commonly held in many dividend growth portfolios.

As with the list on the previous page, we may replace firms held in the Dividend Growth portfolio (see page 5) with companies found in the table below should their dividend growth potential (and/or total return potential) become relatively more attractive than portfolio constituents'.

We find tremendous value in keeping track of dividend growth firms in order to better monitor ideal entry points. We continue to scour our coverage universe for firms to add to our dividend growth watch list, which we update in every edition of our Dividend Growth Newsletter.

DIVIDEND GROWTH WATCH LIST - as of February 1, 2016 (intra-day) Fundamental data as of February 1, 2016

Company Name	Yrly Div's Paid ($) / Shr	Div Yield %	Div Cushion™	Div Safety	Div Growth	Fair Value	VBI Score	Price/Fair Value	Price ($)
3M (MMM)	4.10	2.76%	1.5	GOOD	EXCELLENT	$122.00	4	1.22	148.63
Abbott (ABT)	1.04	2.79%	2.6	GOOD	EXCELLENT	$43.00	6	0.87	37.22
AbbVie (ABBV)	2.28	4.31%	2.0	GOOD	EXCELLENT	$69.00	4	0.77	52.92
ADP (ADP)	2.12	2.57%	5.9	EXCELLENT	EXCELLENT	$94.00	6	0.88	82.48
Analog Devices (ADI)	1.60	2.99%	2.3	GOOD	EXCELLENT	$53.00	3	1.01	53.52
Becton, Dickinson (BDX)	2.64	1.83%	2.7	GOOD	EXCELLENT	$168.00	3	0.86	144.23
Boeing (BA)	4.36	3.63%	2.0	GOOD	EXCELLENT	$119.00	4	1.01	120.13
Chicago Rivet (CVR)	0.72	3.04%	2.6	GOOD	POOR	$28.00	3	0.85	23.69
Coca-Cola (KO)	1.32	3.07%	1.9	GOOD	EXCELLENT	$43.00	4	1.00	43.01
Colgate-Palmolive (CL)	1.52	2.30%	1.6	GOOD	EXCELLENT	$53.00	3	1.25	66.04
Cracker Barrel (CBRL)	4.40	3.28%	1.3	GOOD	GOOD	$132.00	4	1.02	133.99
Deere (DE)	2.40	3.13%	1.3	GOOD	EXCELLENT	$93.00	3	0.83	76.76
Dover (DOV)	1.68	2.91%	1.5	GOOD	EXCELLENT	$61.00	3	0.95	57.78
DuPont (DD)	1.52	2.88%	2.2	GOOD	GOOD	$64.00	5	0.83	52.80
Eli Lilly (LLY)	2.04	2.62%	2.0	GOOD	GOOD	$73.00	3	1.07	77.96
General Dynamics (GD)	2.76	2.09%	3.3	EXCELLENT	EXCELLENT	$127.00	7	1.04	132.25
Genuine Parts (GPC)	2.46	2.98%	1.8	GOOD	EXCELLENT	$83.00	4	0.99	82.56
H&R Block (HRB)	0.80	2.36%	4.4	EXCELLENT	GOOD	$38.00	3	0.89	33.90
Harris (HRS)	2.00	2.31%	1.8	GOOD	EXCELLENT	$89.00	4	0.97	86.48
Honeywell (HON)	2.38	2.35%	2.4	GOOD	EXCELLENT	$95.00	6	1.06	101.10
Hormel Foods (HRL)	1.16	1.43%	2.7	GOOD	EXCELLENT	$56.00	4	1.45	81.00
IBM (IBM)	5.20	4.16%	1.8	GOOD	EXCELLENT	$165.00	3	0.76	125.05
Illinois Tool Works (ITW)	2.20	2.46%	2.1	GOOD	EXCELLENT	$80.00	6	1.12	89.61
Kimberly-Clark (KMB)	3.52	2.74%	1.2	GOOD	GOOD	$106.00	6	1.21	128.37
Lockheed Martin (LMT)	6.60	3.15%	1.4	GOOD	EXCELLENT	$175.00	4	1.20	209.50
Merck (MRK)	1.84	3.65%	2.0	GOOD	GOOD	$55.00	3	0.92	50.41
Northrop Grumman (NOC)	3.20	1.71%	2.4	GOOD	EXCELLENT	$154.00	4	1.22	187.41
Paychex (PAYX)	1.68	3.49%	2.6	GOOD	EXCELLENT	$43.00	6	1.12	48.09
Phillip Morris (PM)	4.08	4.55%	0.5	GOOD	GOOD	$76.00	4	1.18	89.69
Raytheon (RTN)	2.68	2.17%	2.5	GOOD	EXCELLENT	$100.00	4	1.24	123.63
St. Jude (STJ)	1.16	2.19%	3.3	EXCELLENT	EXCELLENT	$67.00	4	0.79	52.96
Texas Instr (TXN)	1.52	2.87%	1.9	GOOD	EXCELLENT	$50.00	3	1.06	53.05
United Technologies (UTX)	2.56	2.94%	1.4	GOOD	EXCELLENT	$105.00	7	0.83	87.11
UPS (UPS)	2.92	3.13%	1.8	GOOD	EXCELLENT	$97.00	7	0.96	93.26
VF Corp (VFC)	1.48	2.36%	2.0	GOOD	EXCELLENT	$55.00	4	1.14	62.83
Walgreens (WBA)	1.44	1.82%	3.0	EXCELLENT	EXCELLENT	$75.00	3	1.05	79.01

UR = Under Review

At any time, our favorite dividend growth ideas are included in the Dividend Growth portfolio, page 5.

Yields to Avoid

By Valuentum Analysts

As many investors know, firms can often become cheap for good reasons. That is, they are not trading cheaply because of Mr. Market's irrational behavior, but instead are trading at depressed levels due to deteriorating underlying fundamental characteristics that actually justify its current share price, even if traditional valuation techniques suggest the firm's shares are inexpensive. On a similar note, firms that boast high dividend yields may do so because the market has little confidence in the sustainability of its dividend and believes a cut may be just around the corner.

Though we fall short of saying the following list of firms will slash their respective dividends anytime soon, our dividend-cut predictive indicator—the Valuentum Dividend Cushion™--indicates that the firms below are at significant risk for a dividend cut in coming years. We think the dividend-growth investor should steer clear of the following firms' shares:

Company Name	Symbol	Industry	Est. Div Yield	Div Safety	Div Cushion
Windstream	WIN	Telecom Services - diversified	9.5%	VERY POOR	-23.1
Range Resources	RRC	Independent Oil & Gas	0.7%	VERY POOR	-22.3
Pioneer Natural Resources	PXD	Independent Oil & Gas	0.1%	VERY POOR	-18.3
Barrick Gold	ABX	Metals & Mining - gold	0.9%	VERY POOR	-15.8
Apache	APA	Independent Oil & Gas	2.3%	VERY POOR	-13.8
D. R. Horton	DHI	Homebuilders	0.9%	VERY POOR	-11.4
Newmont Mining	NEM	Metals & Mining - gold	0.6%	VERY POOR	-11.2
Ryder System	R	Rental and Leasing	3.3%	VERY POOR	-9.4
Textainer	TGH	Rental and Leasing	9.7%	VERY POOR	-9.0
Tidewater	TDW	Energy Equipment	11.2%	VERY POOR	-6.8
Yamana Gold	AUY	Metals & Mining - gold	4.0%	VERY POOR	-6.4
Devon Energy	DVN	Independent Oil & Gas	2.9%	VERY POOR	-6.3
Anadarko	APC	Independent Oil & Gas	2.2%	VERY POOR	-6.1
TAL Intl	TAL	Rental and Leasing	17.6%	VERY POOR	-5.8
Noble Energy	NBL	Independent Oil & Gas	2.2%	VERY POOR	-5.3
MDC	MDC	Homebuilders	3.9%	VERY POOR	-5.2
Cimarex	XEC	Independent Oil & Gas	0.6%	VERY POOR	-5.0
NiSource	NI	Utilities	3.6%	VERY POOR	-4.7
Hess	HES	Refiners	1.9%	VERY POOR	-4.4
Cablevision	CVC	Media - CATV	2.0%	VERY POOR	-4.4
Deltic Timber	DEL	Building Materials	0.7%	VERY POOR	-3.8
Murphy Oil	MUR	Refiners	4.4%	VERY POOR	-3.8
Men's Wearhouse	MW	Retail - Men's, Women's	1.7%	VERY POOR	-3.7
Canadian Natural	CNQ	Independent Oil & Gas	4.0%	VERY POOR	-3.0
Frontier Comm	FTR	Telecom Services - diversified	8.2%	VERY POOR	-3.0
EOG Resources	EOG	Independent Oil & Gas	0.9%	VERY POOR	-2.2
Allegheny Technologies	ATI	Aluminum	4.1%	VERY POOR	-2.2
Huntsman	HUN	Chemicals - broad	4.5%	VERY POOR	-2.0
Time Warner Cable	TWC	Media - CATV	1.7%	VERY POOR	-2.0
PetroChina	PTR	Major Oil & Gas	2.8%	VERY POOR	-1.9
Centurylink	CTL	Telecom Services - diversified	8.1%	VERY POOR	-1.8

The Dividend Cushion Beats the Dividend Aristocrats:
http://www.valuentum.com/articles/20150506

The Valuentum Dividend Cushion™ has an excellent track record of predicting dividend cuts. For more information, please select the following link (login required):

http://www.valuentum.com/articles/20130528

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segments helped offset the organic top-line weakness to a degree, but overall industrial segment operating profit also faced pressure during the quarter, something we would have expected better cost management and higher margins to counteract.

Further, management continues to headline the rather unusual term, 'GE industrial operating + verticals EPS,' and while we like the incremental disclosure, the numbers are starting to drift materially away from core and much more dependable GAAP performance. In the fourth quarter of 2015, for example, 'GE industrial operating + verticals EPS' came in at $0.52 per share, up 27%, while GAAP earnings per share from continuing operations dropped 26%. We don't like the discrepancy, and we believe GE will only get rewarded for its portfolio retransformation when the latter GAAP earnings per share from continuing operations shows material improvement to defend its valuation. The large drop in the measure in the fourth quarter is not exactly encouraging, though we note results continue to be "messy" given recent portfolio transactions.

On a positive note, however, General Electric generated $16.4 billion in cash flow from operating assets in 2015, up 8%, as it drove total industrial and industrial segment margins higher 110 basis points and 80 basis points, respectively. The company's orders grew 3% (1% organically) on a year-over-year basis in the fourth quarter ($13.8 billion versus $13.1 billion), and its backlog grew to an impressive $315 billion (up from $266 billion and +7% organically), though we note some of the incremental expansion includes a contribution from Alstom. During the period, its 'Power' segment generated organic orders growth of 29%, it landed its largest-ever deal in India in its 'Transportation segment,' it won a $600+ million services contract with Cheniere (LNG), and it landed $17 billion in new business from the Dubai airshow. 'Life Sciences' and 'Bioprocessing' continue to be strong areas with its 'Healthcare" division.

Looking ahead to 2016, General Electric is expecting 2%-4% organic revenue growth thanks to a strong backlog and despite a very difficult oil and gas market. Though GE may hit that pace of top-line expansion, we're paying the most attention to operating profit growth, free-cash-flow performance ($29-$32 billion target for 2016), and the firm's ability to execute on cost-cutting initiatives. We'd like to see better operating EPS performance in the GAAP representation of results, and we're looking forward to a much "cleaner" balance sheet once the company completes its financials divestitures. We didn't think GE's fourth-quarter performance was great, but we're willing to get paid a lofty dividend yield (~3.3%) to wait for "cleaner" financials when the time comes. Our fair value estimate remains $30+.

Moody's Puts Oil & Gas and Mining Sectors on Review

By Kris Rosemann

On January 22, Moody's placed 120 oil and gas companies (XLE) from across the globe on review for a credit rating downgrade. The list ranges from massive global producers such as Royal Dutch Shell (RDS.A, RDS.B) and Total (TOT) to nearly 70 US exploration and production and services ("E&P") companies. It also includes 55 mining companies (XLB) that have been punished by the recent rout in commodity prices. Alcoa (AA), Rio Tinto (RIO) and Vale (VALE) are a few notables that made the list for a potential downgrade. The news is not completely unexpected, however, and may likely be a response to several executive teams pointing to legacy (outdated) counterparty/customer ratings as reasons to not be concerned with their own credit quality. We believe Moody's is seeking to correct this.

The credit rating agency recently reduced its crude oil price assumptions due to expectations for continued oversupply in the global oil markets to ensue. Moody's expects Iran to add more than 500,000 barrels per day to global supply, and it anticipates many other players to continue to produce "without restraint" as they battle for market share (or survival, depending on cash flow needs). The rating agency expects US oil producers to cut output in 2016, but not by enough to account for the increase in supply from Iran

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and other unrestrained sources. Moody's now is targeting both Brent crude and West Texas Intermediate crude to average $33 per barrel in 2016, a reduction of $10 per-barrel and $7 per-barrel, respectively (its forecasts call for $38 per barrel in 2017 and $43 per barrel in 2018). We note commercial crude oil inventories in the US remain at 80+ year highs. The credit agency's natural gas price assumptions have not changed.

As can be expected, Moody's points to weakened free cash flow generation as a result of lower realized energy resource prices as the primary reason for reduced credit quality across the E&P space, something the market has been witnessing for some time. The rating agency also noted that projected reductions in capital expenditures by E&P companies will challenge the drilling and oilfield services sector even more than it already has. Moody's expects the drilling and oilfield services sector's EBITDA to drop by another 25%-30% in 2016, and even if commodity prices recover, these companies are not likely to regain pricing power due to the excess production capacity that remains in the sector. Even the largest, most diversified drilling and oilfield services with investment grade credit ratings will see their financial flexibility fall and financial leverage grow; drillers with significant contract expirations are worth watching.

One area that we would have liked to see Moody's pursue is the impact that these downgrades will have on midstream operators (AMLP, AMZ). The events that took place in 2015 revealed the vulnerability of midstream entities to a prolonged downturn in energy resource prices, and we expect the sensitivity to only be heightened as upstream customers suffer potential credit downgrades. Kinder Morgan (KMI) recently announced a large goodwill impairment charge on its core natural gas midstream assets, and operating income performance across the midstream space continues to suffer. The likelihood of many upstream entities to reorganize under Chapter 11 protection in a scenario of an adverse credit event would almost certainly void existing contracts with their midstream counterparts (most pricing would then be renegotiated lower, challenging midstream profit levels). Swift (SFY) marked the 40th E&P to file bankruptcy in the US during this energy market swoon, and there are more to come, with Chesapeake (CHK) being one of the largest that's on the brink. Of the largest pipeline operators, we would not expect Plains All American (PAA) and Energy Transfer Partners (ETP) to retain both investment-grade status and their current distribution levels once this downdraft of the energy cycle has passed.

The 55 mining companies that found themselves on Moody's review-for-downgrade list continue to battle a commodity price collapse due to oversupply and economic weakness in China (FXI) and other BRIC nations, including Brazil (which is in recession). The slowing growth in China, where expansion is at its lowest pace in 25 years, has the potential to bring an unprecedented prolonged downturn in the commodity cycle. Moody's recently downgraded global commodity miner Glencore (GLEN) to one step above junk status as it expects the weak mining market conditions to continue over the next few years. We expect high-yield defaults among the weakest miners to surge as the capacity to service debt wanes. Freeport McMoRan (FCX) is most likely to lose investment-grade status, which had been placed under review for a downgrade earlier this month.

Though Moody's review "focuses on companies rated in the range of A1 to B3," we note the agency included that it is "also reevaluating higher and lower rated companies in the context of industry conditions." ExxonMobil (XOM), Chevron (CVX), ConocoPhillips (COP) and Occidental Petroleum (OXY) were not included on the credit agency's review list. We continue to expect the strongest integrated players to be resilient in the face of weaker energy resource pricing, but dividend growth will likely be sacrificed to ensure balance sheet health. Among the Big 3 majors (XOM, CVX, COP), we point to ConocoPhillips as most at risk for a dividend cut, and its decision to spin off Phillips 66 (PSX) has only punished those opting for the upstream exposure in the face of the collapse in commodity prices. Chevron, ConocoPhillips, and Phillips 66 had previously been holdings in the Dividend Growth Newsletter portfolio, all since removed prior to the energy resource pricing collapse.

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We think the rather sweeping announcement by Moody's is appropriate, even if it may be somewhat late, as many have been calling for a credit review of several of the most overleveraged energy companies since nearly the beginning of the energy resource pricing collapse. That said, we also understand that it is no small action for an NRSRO to cut the credit quality assessment of an entity, which could increase refinancing risks and debt-service costs, ultimately leading to further trouble, if not a credit event. Though most of the bond markets, particularly in high-yield, have already factored in increased default risks across the energy and mining sectors, the looming credit downgrades may finally hit home to the most outspoken skeptics that "we're in a market of lower energy resource pricing for longer." Multi-notch downgrades have not been ruled out.

Lots to Like About Intel's 2016: 3D XPoint and Altera!

By Kris Rosemann

Newsletter portfolio holding Intel (INTC) continues to change with the world around it. An increasingly smart and connected world offers significant opportunities for the company, but those opportunities will not be presented without obstacles to hurdle. It didn't work out so well for the price of Intel the week of its report, as it released a somewhat cautious outlook on a day of a big market swoon, but we still expect some good things ahead from the chip giant. In fact, we continue to like the holding in the context of achieving the goals of the newsletter portfolios.

In the fourth quarter of 2015, results released January 14, Intel reported record revenue of $14.9 billion, though the top line grew a modest 1.3% from the fourth quarter of 2014. The Client Computing Group, which accounted for 59% of total revenue in the quarter, experienced a modest revenue decline as significant pricing strength was unable to offset volume declines of 16%. Intel's Client Computing Group includes platforms designed for desktops, notebooks, tablets, and phones, among other devices. On a year-over-year basis, desktop platform volumes fell 9%, notebook platforms dropped 10%, and tablet volumes plunged 33%. The pressure on volume in this area continues to be expected, but we're viewing the pricing resiliency as a significant "gross-margin-positive" event and a source of upside on a go-forward basis.

The Data Center Group, which includes enterprise and cloud-related platforms, has grown steadily as of late, and the fourth quarter was no exception. Revenue in the group advanced 5% in the quarter to $4.3 billion, a record for the segment, and it now accounts for nearly 29% of revenue. Worth noting in the group was cloud computing growth rates north of 40% on a year-over-year basis in 2015. Expansion in the Data Center Group during the quarter slowed on a year-over-year basis from the 12% leap in the third quarter of 2015 due to "macro weakness," but we are quick to warn of the dangers of putting too much emphasis on any one period's results. The same reasoning goes for the 4.1% quarterly decline in operating income in the segment ($2.17 billion versus $2.27 billion), even as we say we would have still expected segment profit growth, despite the slowing uptick in divisional revenue.

Intel's Internet of Things (IoT) Group is expected to play a growing role in the company's growth story moving forward, though its operating-profit contributions are marginal, all things considered. Nevertheless, the group saw its fourth quarter revenue grow to $625 million from the fourth quarter of 2014, an increase of 6%, which also represented a record for the segment. Though the division currently accounts for less than 5% of the firm's total revenue, the impact of it on Intel's growth story continues to increase. As with the Data Center Group, however, operating income dropped on a year-over-year basis in the fourth quarter, to $132 million from $177 million, revealing some weakness with respect to cost containment during the period.

Perhaps the most compelling growth story in 2015 for Intel was the 20% jump in its Memory business, where $2.5 billion in revenue was generated. Though pricing pressure is always a concern in fast-changing memory operations, Intel and Micron (MU) are preparing to launch into the market a new disruptive technology in 2016, the 3D XPoint nonvolatile memory technology, the industry's first new memory technology in more than two decades. The 3D XPoint technology is said to have "up to 1,000 times lower latency and exponentially greater endurance than NAND." See the video here. Despite collectively only

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accounting for ~40% of Intel's revenue in 2015, the Data Center Group, the IoT Group, and Memory made up for more than 60% of the firm's operating margin. The higher-margin growth opportunities in these businesses are the core of Intel's strategy moving forward.

Though Intel beat expectations on a variety of metrics in the fourth quarter, it was hard to get too excited about consolidated performance. Revenue growth wasn't great, gross margin at the company fell 1.1 percentage points, mostly due to higher unit costs and lower volume. Research and development and marketing, general, and administrative spending was higher than the firm expected in the quarter, and as a percentage of revenue, research and development and marketing, general, and administrative spending grew to 35% of revenue from 33% in the fourth quarter of 2014. The growth in spending Intel undertook in the fourth quarter caused operating income to fall 3% in the quarter to $4.3 billion. Earnings-per-share was flat on a year-over-year basis in the quarter.

Despite the somewhat lackluster fourth-quarter results, Intel remains a strong free cash flow generator. The firm generated ~$19 billion in cash from operations in 2015 while purchasing $7.3 billion in capital assets, resulting in free cash flow of $11.7 billion for the full year, an impressive 21%+ of revenue for the annual period. Though cash from operations declined from 2014 ($20.4 billion), a reduction in capital spending from north of $10 billion in the prior year helped free cash flow grow from $10.3 billion in 2014.

The nearly 14% jump in free cash flow helped the firm increase its cash and investments balance by more than $11 billion to $25.3 billion from the end of 2014 and compares favorably to the company's $22.6 billion total debt level, which increased as a result of $9.5 billion in new long-term debt as part of its Altera acquisition financing plan. We have been huge fans of the Altera acquisition since it was announced:

> By most estimates, the ASIC and ASSP replacement opportunity alone offers growth that's twice as fast as the overall semiconductor industry, something Intel wants, and Altera brings to the table a complete FPGA portfolio (Generation 10), from the Max 10 (refresh CPLD/low-end) to the Arria 10 (mid-range markets), and the Stratix 10 on the high end. Altera estimates that the PLD (FPGA) market was nearly $5 billion in 2014, but the combined portion of the ASIC and ASSP markets that was accessible for PLD displacement was over $50 billion, revealing the tremendous growth potential of PLDs (FPGAs). Altera's Stratix Series already cooperates with Intel 14nm Tri-Gate technology, offering customers double the performance gains in most cases. In a recent Intel presentation, the tech behemoth showcased the significant cost per transistor savings in its 14bnm TriGate technology. The new HyperFlex core fabric architecture results in a level of performance and power efficiency that is unmatched by any existing FPGA architecture, according to the firm.
>
> We like Altera's competitive position to win new business…with Intel, which should smooth deal integration. In fact, Altera's management will tell you that its partnership with Intel has given it an upper hand in addressing performance, power consumption, and cost at the same time, while rivals have struggled with each sequentially. From what we can tell, this has given Altera an early-mover advantage, even relative to its chief FPGA rival Xilinx (XLNX), and the growing "process technology gap" for new designs between PLDs (FPGAs) and the ASIC alternative is revealing. Even if Altera doesn't sustain such an advantage relative to technology-savvy peers, the benefits of FPGAs over ASICs should generate a market large enough for a number of players.

Altera will obviously play a key role in the future of Intel, and we're expecting some big developments toward the latter part of this decade. Looking ahead to 2016, Intel is expecting revenue to grow at a mid-to-high single digit pace on both a GAAP and non-GAAP basis. Gross margin on a GAAP basis is expected to fall 1.6 percentage points, primarily due to non-cash acquisition adjustments related to the Altera transaction. Capital spending for the year is projected to increase to $9.5 billion, revealing the potential for a reduction in free cash flow in 2016, but Altera's free cash flow contributions should

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move the needle (Altera is a cash-generating machine). Cautious comments on China (FXI), however, may mean management is being conservative with its outlook, and we certainly can understand.

All in, we continue to be fans of Intel--it is a holding in both newsletter portfolios--and its ability to continue generating strong free cash flow while its business evolves. A weak PC market will continue to weigh on its largest operating segment, but other growth opportunities are exciting from 3D XPoint to its deal with Altera to upside in mobile with Apple (AAPL). 2015 marked a year showcasing Intel's evolving strategy, and 2016 remains a year of growth as the firm powers the infrastructure of an increasingly smart and connected world. Investors will be watching its growth story closely as they get paid along the way. An annual cash dividend of $1.04 per share translates into a 3.5% dividend yield.

Time to Load Up on Kinder Morgan?

By Brian Nelson, CFA

On January 20, Kinder Morgan (KMI) reported fourth-quarter results, and absent 1) a large goodwill impairment charge related to its core midstream natural gas assets, 2) a reduction to its estimate for backlog of future potential business, and 3) warning that further goodwill impairments are around the corner if energy resource pricing remains depressed, quarterly performance wasn't all that bad (or at least not as bad as some had been expecting). Kinder Morgan had previously announced a 75% dividend cut and a very costly preferred equity issuance just a few weeks ago as it continues to work to get its financial house in order. Our $20 per share fair value estimate is unchanged at this time.

We're starting to like what we're hearing from management, and we again applaud the executive team because we think they understand the issues and are working toward a solution. On the conference call, the team made it very clear to investors that the dividend is not a driver behind the intrinsic valuation of equities, but that it is an output of the free cash flow generating capacity of the entity, or at least it should be. CFO Kim Dang: "I think there is very good financial theory that says whether a company pays a dividend or does not pay a dividend does not impact the value of the firm." If financial advisors and individual investors learn anything from Kinder Morgan's fourth-quarter report, it should be this very important observation. We continue to value Kinder Morgan in the context of an enterprise free cash flow model, which we believe is the best lens through which to evaluate equity value.

Importantly, organically-derived dividends, or those sourced from traditional free cash flow generation, or cash flow from operations less all capital spending and/or earnings, are a symptom of a strong company, not a driver behind it. You wouldn't say, for example, that Apple (AAPL) has been one of the best performers in history because it initiated a dividend a few years ago, would you? Many may not remember that Apple had cut its dividend in 1995… Unlike organically-derived payouts that you would find at Apple or Microsoft (MSFT), for example, dividends that are financed in part from external capital, or from the financing section of the cash flow statement, have little bearing on the underlying valuation of the operating assets of the company, and therefore, should not be used within the valuation context. The dividend discount model is obsolete because it neither considers the net cash on the balance sheet, nor does it consider future enterprise free cash flow generation going forward.

That said, we continue to emphasize that there is a significant difference between traditional free cash flow generation and the industry's definition of "cash flow." These terms are not interchangeable. We define non-GAAP free cash flow as cash flow from operations less all capital spending, and we maintain our view that the industry's definition of "cash flow" is severely imbalanced as it ignores the very growth capital spending that is used to propel net income, which itself is included in the industry's "cash flow" definition. Within any valuation context, the timing of cash inflows and outflows matters, and large growth capital outlays in the near term weigh on intrinsic worth (while rising interest rates challenge the NPV equation in long duration cash flow streams). Under valuation approaches that incorporate the industry's definition of "cash flow" or a financially-engineered dividend, not only are growth capital outlays ignored, but the timing of such capital outlays aren't even a consideration of the analysis. Growth capital is shareholder capital, and it should be factored into the analysis appropriately within the valuation context.

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We continue to await the release of Kinder Morgan's 10-Q, which includes critical and additional information than the data included in the press release, not the least of which is GAAP cash flow from operations. We'll make due with what we have for now. Using net income plus DD&A as a proxy for cash flow from operations, absent working capital shifts during the period, cash flow from operations came in at ~$4.3 billion for the year, based on our estimates. Management noted that growth capital spending in 2015 came in at ~$3.4 billion, and when added to the ~$565 million in sustaining capital spending, gets to ~$3.9 billion in all organic capital spending (excluding acquisitions) for the full year. Until we receive the 10-Q, our estimate is that Kinder Morgan pulled in roughly $400 million in traditional free cash flow during the year, as measured by cash flow from operations (~$4.3 billion) less all capital spending ($3.9 billion). This compares to ~$1.2 billion in future annual dividend obligations on the basis of its $0.50 per share payout on 2.236 billion shares, still implying an organic shortfall, to the tune of ~$800 million.

We posit that this shortfall is why management opted to cut future capital spending by $900 million to help close the gap for 2016 and provide some free-cash-flow cushion for the year. We applaud the executive team for a much more conservative and balanced approach to capital management, and we believe that, absent any exogenous shocks in the energy markets (key customer bankruptcies, ongoing collapse in energy resource pricing, etc), traditional free cash flow generation may very well be sufficient to cover the company's substantially reduced payout during 2016, suggesting that revolving-door trips to the equity and debt markets may be temporarily on hold. Though this is great, management is not leaving much, if any at all, for debt repayment. Backing out impairment "charges" and losses on goodwill "impairments," nearly $1.9 billion in total destroyed shareholder capital, operating income for the full-year came in at $4.5 billion, a modest bump versus last year's mark. However, we're awaiting more clarity about what's included in those charges, and whether we should be completely backing them out for comparison purposes. Was the fourth-quarter the big bath?

In any case, adding the adjusted operating income of $4.5 billion to full-year DD&A of $2.3 billion, Kinder Morgan's reported, adjusted annual EBITDA was $6.8 billion for the full-year. Bear in mind, the $6.8 billion number backs out nearly $1.9 billion of shareholder losses in the form of "charges" that we've analytically pulled below the line. The number differs materially from management's annual mark of ~$7.37 billion disclosed in the press release, which we believe excludes very important and tangible costs backed out from the company's actual, reported income statement provided in its regulatory filings. Though we encourage analysts to evaluate the 10-Q for reported debt figures when it is released, debt, net of cash, stood at $41.2 billion at the end of the year. On the basis of our estimate adjusted EBITDA directly from the income statement, that's good for a net-debt-to-equity mark (or leverage) north of 6 times. Should a corporate, not an MLP, that may not generate any incremental free cash flow for debt repayment (after dividends) be an investment-grade entity leveraged at 6 times?

Furthermore, Kinder Morgan remains exposed to changes in commodity prices, noting key sensitivities in its press release, which may have been less than what many were expecting (perhaps the impairment charges helped out here as well?) -- $7 million in earnings per a $1 change in per-barrel crude oil prices and $1.2 million in earnings per a 0.10 MMBtu change in natural gas. Management is targeting a crude oil price environment of $38 per barrel in 2016 and an average Henry Hub natural gas price of $2.50 per MMBtu. As with Energy Transfer Equity (ETE), the executive team prefers to keep its customer composition tight to the chest, and we posit that there are skeletons in its closet, though perhaps not to the tune of Chesapeake (CHK) and implications on Plains All American (PAA) and Williams Partners (WPZ); we continue to emphasize that the financial health of upstream entities remains critical to the financial health of their midstream counterparts. Kinder Morgan reduced its backlog to the tune of over $3 billion from an estimate just three short months ago and telegraphed that many future opportunities, previously of adequate return, have fallen to the wayside, implying further reductions in total backlog. The environment remains difficult.

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All in, what a difference a few short quarters make. Though we don't yet have the 10-Q in our hands, in our view, Kinder Morgan is in much better shape of covering its dividend in 2016 with traditional free cash flow, as measured by cash flow from operations less all capital spending, and the firm's share price is no longer beholden to an artificial dividend-growth "pricing" paradigm perpetuated by the use of dividend growth models on financially-engineered payouts. We continue to expect other midstream equities to follow Kinder Morgan's lead in more conservatively managing their capital allocation decisions, and that may mean further distribution cuts across the MLP space to come. Kinder Morgan's shares are rallying on this news, and other executive teams are watching. Our fair value estimate for Kinder Morgan remains unchanged at $20 per share. We would expect the credit rating agencies to negatively reevaluate Kinder Morgan's credit outlook in the event the dividend is increased or share buybacks are pursued anytime soon, especially without support from the capital markets, which may not be had unless energy resource pricing recovers materially.

Microsoft!

By Brian Nelson, CFA

If there is any stock that you might think of when you think of Valuentum, it probably is Microsoft (MSFT). The software giant put up fantastic fiscal second-quarter (calendar fourth-quarter) results after the close January 28. Kudos to my University of Chicago Booth School of Business "colleague," Microsoft CEO Satya Nadella. Things have really taken off since he took the helm in February 2014.

Microsoft is one of the largest holdings in the Dividend Growth Newsletter portfolio, and it has been one of the best-performing equities since registering a high rating on the Valuentum Buying Index. The company also has been the "focus" income idea in nearly every one of Valuentum's dividend growth presentations to interested attendees at meetings of the American Association of Individual Investors (AAII) from Cleveland to Silicon Valley and beyond. It hasn't been a few days since we walked through Microsoft's discounted cash-flow valuation model in the latest edition of our 'Financial Analysis Statement' seminar.

Microsoft beat both revenue and non-GAAP earnings-per-share estimates in the quarter, the latter by nearly 10%, simply a large level of outperformance for a company of Microsoft's size. On a constant-currency basis, non-GAAP revenue advanced 3% in the period, while the firm "delivered double-digit operating income growth." Revenue in its 'Productivity and Business Processes' and 'Intelligent Cloud" increased 5% and 11% on a constant-currency basis, respectively, while sales in its 'Personal Computing' segment fell 2% after adjusting for currency changes. Management commented favorably about strong holiday momentum by Surface and Xbox.

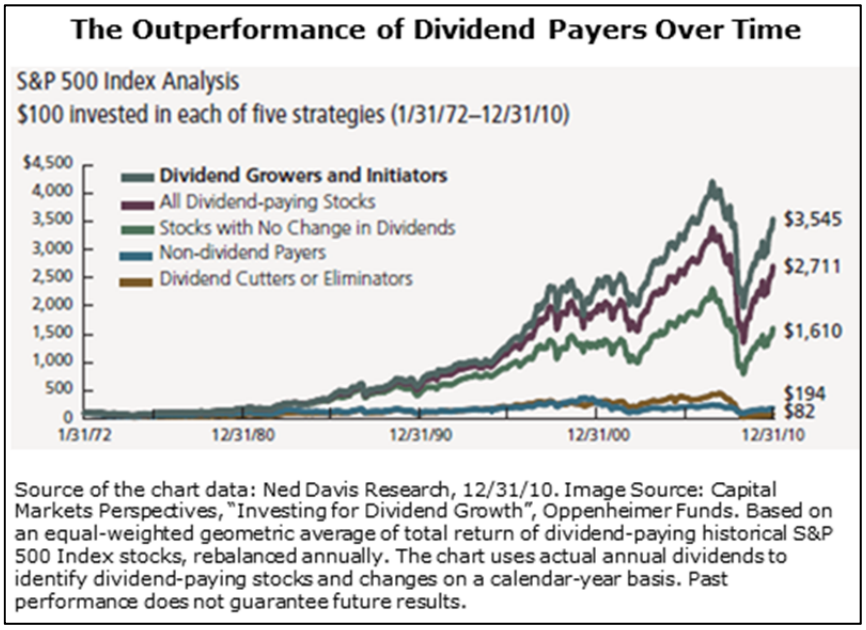
Through the first six months of the fiscal year, cash flow from operations at Microsoft advanced 12% on a year-over-year basis, to $14.2 billion. Free cash flow came in at $10.8 billion, better than the $9.9 billion mark in the six-month period in last fiscal year, despite increased capital investment. The company's total cash balance advanced to $102.6 billion, trumping its $44.4 billion long and short-term debt load, good enough for $58.2 billion in net cash (~$7.25 per share). Annualizing Microsoft's $0.78 earnings-per-share mark in the most recently-reported quarter and backing out the company's net cash implies Microsoft is trading at less than 15 times earnings on the basis of yesterday's closing price.

No longer exchanging hands at as large of a discount to intrinsic value as they once had, Microsoft's shares have converged to our estimate of their intrinsic value, $55 per share, more than double the price at which they were added to the Dividend Growth Newsletter portfolio. The company yields ~2.8%, and its Dividend Cushion ratio remains rock-solid. We're expecting ongoing strength at the software giant, and we're inclined to let this winner "run" as we collect dividend payments.

About the Valuentum Dividend Cushion™

By Valuentum Analysts

History has revealed that the best performing stocks during the previous decades have been those that shelled out ever-increasing cash to shareholders in the form of dividends. In a recent study, S&P 500 stocks that initiated dividends or grew them over time registered roughly a 9.6% annualized return since 1972 (through 2010), while stocks that did not pay out dividends or cut them performed poorly over the same time period.



Source of the chart data: Ned Davis Research, 12/31/10. Image Source: Capital Markets Perspectives, "Investing for Dividend Growth", Oppenheimer Funds. Based on an equal-weighted geometric average of total return of dividend-paying historical S&P 500 Index stocks, rebalanced annually. The chart uses actual annual dividends to identify dividend-paying stocks and changes on a calendar-year basis. Past performance does not guarantee future results.

Such analysis is difficult to ignore, and we believe investors may be well-rewarded in future periods by finding the best dividend-growth stocks out there. As such, we've developed a rigorous dividend investment methodology that uncovers firms that not only have the safest dividends but also ones that are poised to grow them long into the future.

How did we do this? Well, first of all, we scoured our stock universe for firms that have cut their dividends in the past to uncover the major drivers behind the dividend cut. This is what we found out: The major reasons why firms cut their dividend had to do with preserving cash in the midst of a secular or cyclical downturn in demand for their products/services or when faced with excessive leverage (how much debt they held on their respective balance sheets).

The Importance of Forward-Looking Dividend Analysis

Armed with this knowledge, we developed the forward-looking Valuentum Dividend Cushion™, which is a ratio that gauges the safety of a dividend over time.

Most dividend analysis that we've seen out there is backward-looking – meaning it rests on what the firm has done in the past. Although analyzing historical trends is important, we think assessing what may happen in the future is even more important. The S&P 500 Dividend Aristocrat List, or a grouping of firms that have raised their dividends for the past 25 years, is a great example of why backward-looking analysis can be painful. One only has to look over the past few years to see the removal of well-known names from the Dividend Aristocrat List (including General Electric and Pfizer) to understand that backward-looking analysis is hardly worth your time. After all, you're investing for the future, so the future is all you should care about.

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We want to find stocks that will increase their dividends for 25 years into the future, not use a rear-view mirror to build a portfolio of names that may already be past their prime dividend growth years. The Valuentum Dividend Cushion™ measures just how safe the dividend is in the future. It considers the firm's net cash on its balance sheet (cash and cash equivalents less debt) and adds that to its forecasted future free cash flows (cash from operations less capital expenditures) and divides that sum by the firm's future expected dividend payments. At its core, it tells investors whether the firm has enough cash to pay out its dividends in the future, while considering its debt load. If a firm has a Valuentum Dividend Cushion™ above 1, it can cover its dividend, but if it falls below 1, trouble may be on the horizon.

In our study, the Valuentum Dividend Cushion™ process caught every dividend cut made by a non-financial, operating firm that we have in our database, except for one (Marriott). But interestingly, the Valuentum Dividend Cushion™ indicated that Marriott should have never cut its dividend, and sure enough, two years after the firm did so, it raised it to levels that were higher than before the cut.

Here are the results of the study (a Valuentum Dividend Cushion™ below 1 indicates the dividend may be in trouble). The Valuentum Dividend Cushion™ score shown in the table below is the measure in the year before the firm cut its dividend, so it represents a predictive indicator. The measure continues to do well by members in real-time as well (beyond the constraints of any academic study).

The Valuentum Dividend Cushion Caught These Dividend Cuts in Advance

A Valuentum Dividend Cushion Score Below 1 Indicates a Firm's Dividend is At Risk in the Years Ahead

Dividend Cutter	Cut Date	Dividend Cushion (Before Cut)	Reason for Dividend Cut
Avery Dennison (AVY)	31-Jul-09	0.66	Reduced dividend to support debt-reduction efforts.
ConAgra Foords (CAG)	16-Mar-06	-0.59 (1)	Restructuring, divestitures.
Constellation (CEG)	18-Feb-09	-4.36	Refocus on core business of generating and selling power.
DR Horton (DHI)	6-May-08	-0.03	Housing turmoil.
Gannett Co. (GCI)	25-Feb-09	-0.06	Excessive debt; preserve cash amid downturn of newspaper industry.
La-Z-Boy (LZB)	17-Feb-09	0.89	Suspended dividend to preserve cash amid downturn in home furnishings.
Marriott Intl (MAR)	1-May-09	2.18 (2)	Suspended dividend in the wake of weak business travel, but dividend achieved record highs again, May 6, 2011.
Masco Corp (MAS)	11-Feb-09	-0.74	Cut dividend to ensure ability to fund operations and service debt coming due.
New York Times (NYT)	20-Nov-08	0.04	Effort to preserve cash. Downturn in newspaper industry. Loss of investment-grade credit rating.
Pfizer (PFE)	26-Jan-09	0.54	Bought Wyeth to diversify revenue base. Raised $22 billion+ in debt.
Sara Lee Corp (SLE)	8-Aug-06	0.70	Streamlining operations, business unit divestitures to raise cash.
Sunoco Inc. (SUN)	6-Oct-09	-0.85 (3)	Poor margins, overseas competition.
SuperValu (SVU)	20-Oct-09	-5.78	Rising unemployment, competition from Wal-Mart, etc.
Valero Energy (VLO)	27-Jan-10	0.15	Lower demand for gas and diesel.
Vulcan Materials (VMC)	14-Oct-11	-1.42	Free up much-needed cash amid downturn in aggregate demand.

(1) Forecast period for ConAgra, 2007 through 2011.

(2) Marriott is an instance where management prematurely cut its dividend, in our opinion. The Cushion reflected little risk at the time of cut, and sure enough Marriott restored its payout to record high

(3) Forecast adjusted to reflect Sunoco's poor free cash flow trends by end last reported year.

Backtesting Methodology: Net balance sheet (1 year prior to dividend cut). Free cash flow for years beginning in year of dividend cut through reported years. If reported years do not total five, last reported year is extrapolated for remainder of forecast period. Dividends paid reflects what the dividends would be ex dividend cut.

At the very least, using the Valuentum Dividend Cushion™ can help you avoid firms that are at risk of cutting their dividends in the future. And we are the only firm out there that does this type of in-depth analysis for you. We provide the Valuentum Dividend Cushion™ score in the dividend reports and monthly Dividend Growth Newsletter, and we also scale the safety of a firm's dividend based on this measure in simple terms: Excellent, Good, Poor, Very Poor.

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Here's a glimpse of the Valuentum Dividend Cushion™ score (as of November 2011) for a sample set of firms in our coverage universe. Please note that the current score on these and hundreds more are available with a membership to our website:

Company Name	Dividend Cushion
Abbott Labs (ABT)	2.3
Coca-Cola (KO)	1.9
Family Dollar (FDO)	4.4
International Business Machines (IBM)	3.7
Johnson & Johnson (JNJ)	2.5
Merck (MRK)	2.5
Molex (MOLX)	2.5
Pepsi (PEP)	1.3
Proctor & Gamble (PG)	1.4
Wal-Mart (WMT)	1.4

Subscribe to Valuentum to monitor the Dividend Cushion of firms you own.

Understanding Dividend Growth

It takes time to accumulate wealth through dividends, so dividend growth investing requires a long-term perspective. We assess the long-term future growth potential of a firm's dividend, and we don't take management's word for it. Instead, we dive into the financial statements and make our own forecasts of the future to see if what management is saying is actually achievable. We use the Valuentum Dividend Cushion™ as a way to judge the capacity for management to raise its dividend – how much cushion it has – and we couple that assessment with the firm's dividend track record, or management's willingness to raise the dividend.

In many cases, we may have a different view of a firm's dividend growth potential than what may be widely held in the investment community. That's fine by us, as our dividend-growth investment horizon is often longer than others'. We want to make sure that the firm has the capacity and willingness to increase the dividend years into the future and will not be weighed down by an excessive debt load or cyclical or secular problems in fundamental demand for their products/services. We scale our dividend-growth assessment in an easily-interpreted fashion: Excellent, Good, Poor, Very Poor.

What Are the Dividend Ideas We Seek to Deliver to You in Our Newsletter?

First of all, we're looking for stocks with dividend yields that are greater than the average of the S&P 500, or about 2% (but preferably north of 3%). This excludes many names, but we think such a cutoff eliminates firms whose dividend streams aren't yet large enough to generate sufficient income. Second, we're looking for firms that register an 'EXCELLENT' or 'GOOD' rating on our scale for both safety and future potential growth. And third, we're looking for firms that have a relatively lower risk of capital loss, as measured by our estimate of the company's fair value.

The Valuentum Dividend Cushion™ has an excellent track record of predicting dividend cuts. For more information, please select the following link (login required):

http://www.valuentum.com/articles/20130528

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Excerpt from *The 13 Steps to Understand the Stock Market*

Step #12: **Valu**e and Mom**entum** Outperform Everywhere

Momentum is the biggest embarrassment to efficient markets (according to the "father of modern finance" and Nobel laureate in Economics, Eugene Fama), academic research continues to conclude that 'Value and Momentum' combined outperform in every market across every asset class, and we continue to demonstrate empirical evidence of the superiority of a combined value-momentum process in the portfolio of our Best Ideas Newsletter. Key takeaway: Value and momentum combined outperform in every market across every asset class.

-- The **Valu-entum** Team

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Fair Value Range. The fair value range represents an upper bound and lower bound, between which we would consider the firm to be fairly valued. The range considers our estimate of the firm's fair value and the margin of safety suggested by the volatility of key valuation drivers, including revenue, gross margin, earnings before interest, and enterprise free cash flow (the determinants behind our ValueRisk™ rating).

ValueRisk™. This is a proprietary Valuentum measure. ValueRisk™ indicates the historical volatility of key valuation drivers, including revenue, gross margin, earnings before interest, and enterprise free cash flow. The standard deviation of each measure is calculated and scaled against last year's measure to arrive at a percentage deviation for each item. These percentage deviations are weighted equally to arrive at the corresponding fair value range for each stock, measured in percentage terms. The firm's performance is measured along the scale of LOW, MEDIUM, HIGH, and VERY HIGH. The ValueRisk™ rating for each firm also determines the fundamental beta of each firm along the following scale: LOW (0.85), MEDIUM (1), HIGH (1.15), VERY HIGH (1.3).

Dividend Track Record. We assess each firm's dividend track record based on whether the fundamentals of the firm have ever forced it to cut its dividend. If the firm has ever cut its dividend (within the last 10 years), we view its track record as RISKY. If the firm has maintained and/or raised its dividend each year (over the past 10 years), we view its track record as HEALTHY.

Dividend Safety. We measure the safety of a firm's dividend by adding its net cash to our forecast of its future cash flows and divide that sum by our forecast of its future dividend payments. This process results in a ratio called the Dividend Cushion™. Scale: Above 2.75 = EXCELLENT; Between 1.25 and 2.75 = GOOD; Between 0.5 and 1.25 = POOR; Below 0.5 = VERY POOR.

Valuentum Dividend Cushion™. This is a proprietary Valuentum measure that drives our assessment of the firm's Dividend Safety rating. The forward-looking measure assesses dividend coverage via the cash characteristics of the business.

Dividend Growth Potential. We blend our analysis of a firm's Dividend Safety with its historical Track Record, while also considering historical dividend growth trends. We believe such a combination captures a firm's capacity (cash flow) and willingness (track record) to raise its dividend in the future. Scale: EXCELLENT, GOOD, POOR, VERY POOR.

Risk of Capital Loss. We think capital preservation is key for the dividend investor. As such, we evalute the risk of capital loss by assessing the intrinsic value of each firm based on our discounted cash-flow process. If a firm is significantly OVERVALUED, we think the risk of capital loss is HIGH. If a firm is FAIRLY VALUED, we think the risk of capital loss is MEDIUM, and if a firm is UNDERVALUED, we think the risk of capital loss is LOW.

Dividend Strength. Our assessment of the firm's dividend strength is expressed in a matrix. If the safety of a firm's dividend is EXCELLENT and its growth prospects are also EXCELLENT, it scores high on our matrix (top right). If the firm's dividend safety and the potential future growth are VERY POOR, it scores lower on our scale (bottom left).

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