OUR DIVIDEND GROWTH NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

July 1, 2016
Volume 5 Issue 7

Valuentum Securities Inc.
www.valuentum.com info@valuentum.com

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
13.6%	Mid-High Single Digits	6.1pts

*Please see note below regarding performance measurement.

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"Individual investors and financial advisors deserve better: the truth."
– 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, July 1, 2016, the portfolio is significantly exceeding this goal.

Distributing Truth on MLPs

By Kris Rosemann and Brian Nelson, CFA

The recent merger break-up fiasco at Energy Transfer Equity (ETE) and Williams Companies (WMB) has put the master limited partnership (MLP) conversation back into the spotlight, after the two entities were unable to finalize a merger that had been announced in fall 2015 and would have created the largest pipeline company in the US. The deal between Energy Transfer Equity and Williams was officially terminated by Energy Transfer Equity June 29 after a court ruled that the firm was legally able to walk away from the agreement when it was unable to deliver an opinion on the tax treatment of the transaction that was required by June 28. Williams has since stated that it will seek monetary damages from ETE for the failed transaction.

Brian Nelson, CFA
President, Equity Research
brian@valuentum.com

Kris Rosemann
Associate Investment Analyst
kris@valuentum.com

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

Latest Dividend Growth Portfolio Alerts

Today: Talen (TLN) removed

June 24: Closed 4 contracts of SPY put options (Jun exp, $200 strike)

June 13: Removed 77 shares of MSFT at $50.18

All email transaction alerts are emailed from the account info@valuentum.com.

Updated June 30, 2016 - Calendar 2015 - $ mil

	Adjusted Reported EBITDA	Cash from Operating Activities (CFO)	Total Capital Expenditures	Dividends, Distributions	Free Cash Flow after Dividends, Distributions	Net Debt	Net Debt/ Adjusted EBITDA
Energy Transfer Equity (ETE)	4,817.0	3,068.0	-9,386.0	-3,425.0	-9,743.0	36,362.0	7.5
Kinder Morgan (KMI)	6,825.0	5,303.0	-3,896.0	-4,258.0	-2,851.0	42,998.0	6.3
Spectra Energy (SE)	2,546.0	2,247.0	-2,848.0	-1,194.0	-1,795.0	13,331.0	5.2
Williams Co (WMB)	3,062.0	2,678.0	-3,167.0	-2,778.0	-3,267.0	23,888.0	7.8
Boardwalk Pipeline (BWP)	719.9	576.4	-374.5	-101.5	100.4	3,456.2	4.8
Buckeye Partners (BPL)	825.4	710.2	-594.5	-604.9	-489.3	3,839.4	4.7
CONE Midstream (CNNX)	131.4	116.0	-291.2	-52.1	-227.3	73.3	0.6
DCP Midstream (DPM)	349.0	650.0	-281.0	-487.0	-118.0	2,422.0	6.9
Energy Transfer (ETP)	4,527.0	2,747.0	-9,098.0	-3,674.0	-10,025.0	28,385.0	6.3
EnLink Midstream (ENLK)	654.5	645.6	-572.3	-545.8	-472.5	3,083.9	4.7
Enterprise Products (EPD)	5,056.2	4,002.4	-3,830.7	-2,991.7	-2,820.0	22,655.7	4.5
EQT Midstream Partners (EQM)	489.4	463.5	-409.0	-236.1	-181.6	441.6	0.9
Genesis Energy (GEL)	307.0	289.5	-495.8	-257.3	-463.6	2,911.2	9.5
Magellan Midstream (MMP)	1,130.4	1,069.7	-621.2	-662.9	-214.4	3,410.9	3.0
Plains All American (PAA)	1,694.0	1,344.0	-2,079.0	-1,671.0	-2,406.0	11,347.0	6.7
Spectra Energy Partners (SEP)	1,568.0	1,522.0	-1,883.0	-992.0	-1,353.0	5,960.0	3.8
Summit Midstream Partners (SMLP)	215.5	166.0	-118.1	-152.1	-104.2	924.6	4.3
Tallgrass Energy Partners (TEP)	281.4	289.3	-65.4	-187.0	36.9	751.4	2.7
Western Gas Partners (WES)	795.8	669.6	-602.3	-557.3	-490.0	2,609.3	3.3
Chevron (CVX)		19,456.0	-29,504.0	-8,120.0	-18,168.0	27,180.0	
ConocoPhillips (COP)		7,572.0	-10,050.0	-3,664.0	-6,142.0	22,512.0	
ExxonMobil (XOM)		30,344.0	-26,490.0	-12,260.0	-8,406.0	34,982.0	
Apple (AAPL)[1]		81,266.0	-11,247.0	-11,561.0	58,458.0	-149,703.0	
Microsoft (MSFT)[2]		29,080.0	-5,944.0	-9,882.0	13,254.0	-63,733.0	
MasterCard (MA)		4,043.0	-177.0	-727.0	3,139.0	-3,451.0	

(1) Fiscal year ended Sept. 30, 2015
(2) Fiscal year ended June 30, 2015

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Distributing Truth on MLPs…**from previous page**

We have been warning of the dangers of a tie up of the two entities that are both so overleveraged, and it has become evident that disagreements at the top of both Williams and Energy Transfer Equity have led to a significant shakeup in their management teams and boards of directors. On June 30, nearly half of Williams' directors resigned after failing to oust CEO Alan Armstrong, who was an opponent of the merger, and Energy Transfer Equity CFO Jamie Welch, who has been quoted referencing the deal terms as "mutually assured destruction," was released from his duties in early February. We can only imagine how much finger-pointing had been going on, and the activity by the Williams' board following the failed transaction seems like mutiny, at least from our perspective. How can investors believe that a board that is so fast to dissolve is acting in their best interests? It's very concerning from a corporate governance standpoint, and something tells us this isn't the last we've heard about the ETE-WMB tie-up. Things could still get ugly.

Despite the news of the failed attempted merger, the near-term outlook for most midstream MLPs has improved since early 2016. The most transparent positive is improvement in the energy resource pricing markets, as the recent bounce in crude oil prices has alleviated some of the pressure pipeline operators had been experiencing. Remember when others were saying midstream equities were immune to commodity-price changes? How wrong they were. Additionally, the vast majority of midstream MLP firms are not exposed to the uncertainty surrounding 'Brexit' and ongoing concerns over economic growth in Asia, specifically China. Most recently, the former of these two concerns has had an impact on the yields on government bonds in developed countries across the globe (US 10-year Treasury bond yields fell to record lows July 1) as risk-averse investors attempt to avoid such uncertainty. This dynamic has only increased the demand for high-yielding stocks for income-oriented investors, and pipeline companies have traditionally fit this bill nicely, especially when considering their general lack of exposure to *global* economic uncertainty, even if energy market uncertainty is still prevalent.

Falling US Treasury bond yields coupled with the reduced probability of additional federal fund rate increases by the Fed in 2016 thanks in part to 'Brexit' uncertainty may provide more "hot air" to inflate those equities employing the MLP business model via the ongoing easing of access to the capital markets. Can you believe it? Spreads on some of the lowest-rated (highest-yielding) debt, for example, have improved drastically since the near term peak earlier this year. As we have been articulating for some time now, MLPs are far too dependent on the capital markets (i.e. issuance of new debt and equity capital) for them to be considered rock-solid, independently sustainable entities. However, as long as the debt and equity markets remain open to them to provide the financing cash flow generation to cover cash distributions, most MLPs will continue to be able to operate in their current form as dividend-hungry investors bid up shares on the basis of yield considerations, despite what we consider to be egregious business-model risk (promulgated by regulations that favor MLPs over traditional corporates).

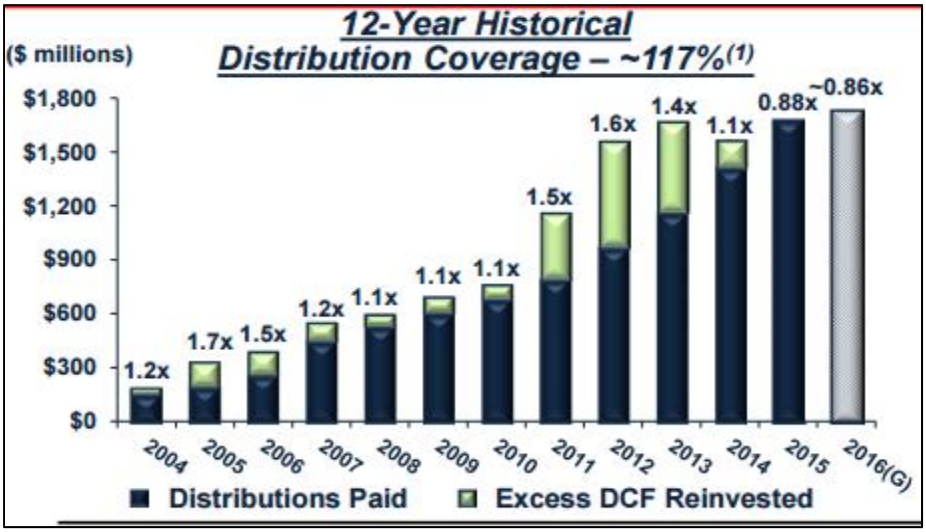

Image source: PAA 2016 Investor Day presentation

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Let's take a quick anecdotal look at Plains All American (PAA) to illustrate what we mean, for example. The MLP expects its expansion capital spending to be funded by at least 55% new equity, as well as excess "cash flow." However, excess "cash flow" may be hard to come by as it projects its distributable cash flow distribution coverage to be well below 1 for the second consecutive year. (The chart on the previous page provides a visual representation of the firm's distribution "coverage," or better yet lack of it.) You might say – "this is ridiculous." How can Plains All American keep paying out this distribution when even its own measures of internal cash flow before capital outlays related to growth spending are coming up short?

The answer is quite simple – ever more debt, more equity. Plains All American is not only admitting it will issue more equity in a bid for growth, but it recently floated a sophisticated convertible offering, which also came to the rescue of the distribution. It's almost as though operating performance doesn't matter within the MLP universe as much as access to new capital does--if an MLP can float more debt and equity, all will be well. If it can't, trouble is on the horizon. This is what makes handicapping the MLP space so difficult for investors; in many cases, credit access and energy resource pricing trump firm-specific operating fundamentals. Industry veterans have a hard time accepting this fact.

The question on most investors' minds, however, is how long the MLP merry-go-round will last (i.e. how long MLPs will be able to continue such an external-capital, self-perpetuating cycle without a massive fallout). Executive teams of MLPs are aware of the vulnerabilities of their business models, perhaps punctuated by Kinder Morgan's (KMI) roll-up many moons ago. More recently, however, Plains All American, acknowledged the many flaws of the MLP business model, if not explicitly then indirectly via a discussion of the viability of the long-term sustainability of the MLP model. In its 2016 Investor Day presentation, the entity stated that it will continue to evaluate structure simplification alternatives, specifically a simplification transaction between PAA and its general partner. To us, this in itself is an acknowledgement from a major player in the MLP space that changes are necessary in its corporate structure.

Even if energy resource pricing has offered a nice reprieve, the vulnerabilities of the MLP business model have been exposed. If the examples of Kinder Morgan and Plains All American weren't enough, in late 2015, Targa Resources (TRGP) rolled up Targa Resource Partners, and around the same time, Sempra Energy (SE) backtracked on its plans to form an MLP. The path to recent distribution cuts across the MLP space have been devastating for many: NGL Energy Partners (NGL), American Midstream Partners (AMID), and Crestwood Equity Partners (CEQP) all cut their distributions in April 2016, and Southcross Energy Partners (SXE) cut its distribution in January 2016. More than 20 MLPs cut distributions in 2015, and most of those cuts came from smaller MLPs, which may be telling of the fragility and shaky future of this business model. Many know that Boardwalk Pipeline (BWP) cut its distribution in February 2014, and now-bankrupt LINN Energy's distribution cuts were foretold by the entity's abysmal Dividend Cushion ratio. Even the ALPS Alerian MLP ETF (AMLP) cut its quarterly dividend ~20%.

During its investor day, Plains All American also highlighted a number of changes it expects to come in its operating environment over the near-term and intermediate/long-term time horizons, both of which it expects to be very different from what we have seen in recent years. The energy boom following the Great Recession of late last decade drove unbridled growth in the businesses and assets in the MLP universe, causing the overall quality of the space to deteriorate significantly, and as a result of quantitative easing and lax monetary policy, a large number of MLPs became dependent on unrestrained access to low costs of capital. This is where things will begin to change. Relative to the "good old days," it has become much more difficult for MLPs to fund their growth projects, forcing them to look elsewhere for sources of expansion. A renewed focus on rationalization and optimization can be expected, but this will bring increased competition, meaning that many of the smaller MLPs that benefitted from the ease of access to low costs of capital may become competitively disadvantaged as larger operators with higher-quality assets benefit from scale and capacity utilization on existing infrastructure.

Midstream pipeline MLPs are also expected to look to industry consolidation and asset acquisitions as sources of growth as large organic growth capital programs will become a thing of past the for much of the

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space. However, the recent implosion of the ETE-WMB tie-up brings the viability of such a strategy into question. While the two firms are among the most-leveraged in the industry, many others are not far behind (see chart at top of article). Perhaps the best-case scenario for MLPs then is exactly what Plains All American has hinted at in its Investor Day presentation: a consolidation of it and its general partner. Such a move would reduce its dependence on the capital markets, and it may be the best way for the firm to remain a legitimately healthy operator over the long term. After all, the very pioneer of the MLP business model, Kinder Morgan, has abandoned it. We have long been positive on the underlying businesses of the midstream space, but the MLP business/financial model fouls up the investment prospects of the industry, in our opinion.

We expect the MLP business/financial model to eventually be reevaluated at the highest regulatory levels and deemed an "unfair" structure. That MLPs can recirculate capital raised from the financial markets (financing section of the cash flow statement) to pay distributions, which are widely followed by "trusting" investors and often used to value their equities is incredible. How can you be sure that our perspective is worth considering? **Ask one question: what would happen to MLPs if the capital markets shut down?** The answer: They would have to cut their distributions as cutting off growth and investment would be a bonehead move in light of potential positive NPV projects. In any business seeking to generate value for shareholders, which all are, investment growth capital therefore will always be funded first and foremost through a company's operating cash flow, and since most capital investment and dividends, collectively, overwhelm operating cash flow generation (as in the chart above), most all MLP payouts are in part financially-engineered (i.e. supported by the financing section of the cash flow statement). External capital is not the primary source of growth funding.

Though it may not happen anytime soon, we believe there will eventually be an "investor-led" crusade against this dangerous business model. Such opposition doesn't necessarily have to come from investors either. It could come from a corporate coalition. There are many corporates, for example, that have decent balance sheets and cover their dividends with traditional free cash flow, but have much less sanguine credit marks by the agencies relative to those of such overleveraged, "cash-burning" (after dividend payments) pipeline MLP plays. Moreover, we believe the SEC should take a hard look at the industry's definition of "cash flow," which we believe is very misleading to even the most sophisticated investors. In particular, an MLP's definition of distributable cash flow excludes the very growth capital spending that drives net income, which itself is included in the calculation of distributable cash flow. When analysts use distributable cash flow in valuation, they, by its very own definition, exclude a portion of the cash capital outflows (shareholder money) that are used to drive net income higher, a severe imbalance in the valuation equation.

Individual investors and financial advisors deserve better: the truth.

Microsoft Position Halved

From "What?!? Microsoft Acquires LinkedIn; NO!" June 13, 2016:

It's almost hard to believe that Microsoft (MSFT) CEO Satya Nadella would throw ~$26.2 billion of cash in the form of shareholder capital that could potentially go toward one of the best future dividend growth streaks in history at a large, Internet-based acquisition such as LinkedIn (LNKD), but it happened June 13. Unbelievable. We think most of the news outlets had to do a double-take before reporting the news (we did, too), and we're not surprised that Microsoft's shares are selling off on the announcement. Some are painting the deal optimistically, but we're bummed out. We're removing half of our position in Microsoft from the Dividend Growth Newsletter portfolio on the news at ~$50.18 per share for one of the biggest gains in the newsletter portfolio yet.

The Dividend Growth Portfolio

Annualized Return	Annualized Goal	Outperformance
13.6%	Mid-High Single Digits	6.1pts

DIVIDEND GROWTH PORTFOLIO -- as of July 1, 2016 — 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	69.02	6,971.02	4.0%	228.26
Apple (AAPL)	7/24/2013	63.17	51	3,228.45	95.89	4,890.39	2.8%	116.28
Cisco (CSCO)	11/14/2014	26.31	199	5,242.53	28.80	5,731.20	3.3%	206.96
Coach (COH)	9/19/2014	37.55	80	3,011.00	40.73	3,258.40	1.9%	108.00
Cracker Barrel (CBRL)	2/1/2016	133.50	18	2,410.00	169.69	3,054.42	1.7%	82.80
Energy Sector SPDR (XLE)	4/1/2015	72.63	121	8,795.76	68.60	8,300.60	4.7%	262.33
General Electric (GE)	10/21/2013	26.18	240	6,290.20	31.49	7,557.60	4.3%	220.80
Hasbro (HAS)	12/30/2011	31.89	110	3,514.90	83.90	9,229.00	5.3%	224.40
Intel (INTC)	12/30/2011	24.25	289	7,015.25	32.75	9,464.75	5.4%	300.56
Johnson & Johnson (JNJ)	12/30/2011	65.58	107	7,024.06	121.29	12,978.03	7.4%	342.40
Medtronic (MDT)	12/30/2011	38.25	157	6,012.25	87.03	13,663.71	7.8%	238.64
Microsoft (MSFT)	12/30/2011	25.96	77	2,005.92	51.16	3,939.32	2.2%	110.88
Proctor & Gamble (PG)	12/30/2011	66.71	105	7,011.55	84.78	8,901.90	5.1%	281.40
PP&L (PPL)	12/30/2011	29.42	238	7,008.96	37.60	8,948.80	5.1%	361.76
Realty Income (O)	7/24/2013	44.35	60	2,668.00	69.64	4,178.40	2.4%	143.40
S&P Dividend ETF SPDR (SDY)	4/20/2016	81.33	105	8,546.65	84.03	8,823.15	5.0%	212.64
Vanguard REIT ETF (VNQ)	2/1/2016	77.07	32	2,473.24	88.70	2,838.40	1.6%	105.87
Latest changes: Sold TLN, closed SPY put options; sold half of MSFT.								
Cash -- changes in monthly cash balance reflects dividends received and trading				2,363.42		52,802.73	30.1%	3,547.38
Dividend Growth Portfolio				100,000.00		**175,531.82**	100.0%	**TBD**

DG Portfolio Annualized Return (from inception through current date)	**13.6%**
DG Portfolio Annualized Return Goal (Mid-to-High Single Digit Returns)	7.5%
DG Portfolio Annualized Return Outperformance	**6.1%**
SPDR S&P Dividend ETF (SDY)	**13.3%**

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 July 1, 2016. Cost basis includes commissions. Results include divdends, but no interest received on cash balance.

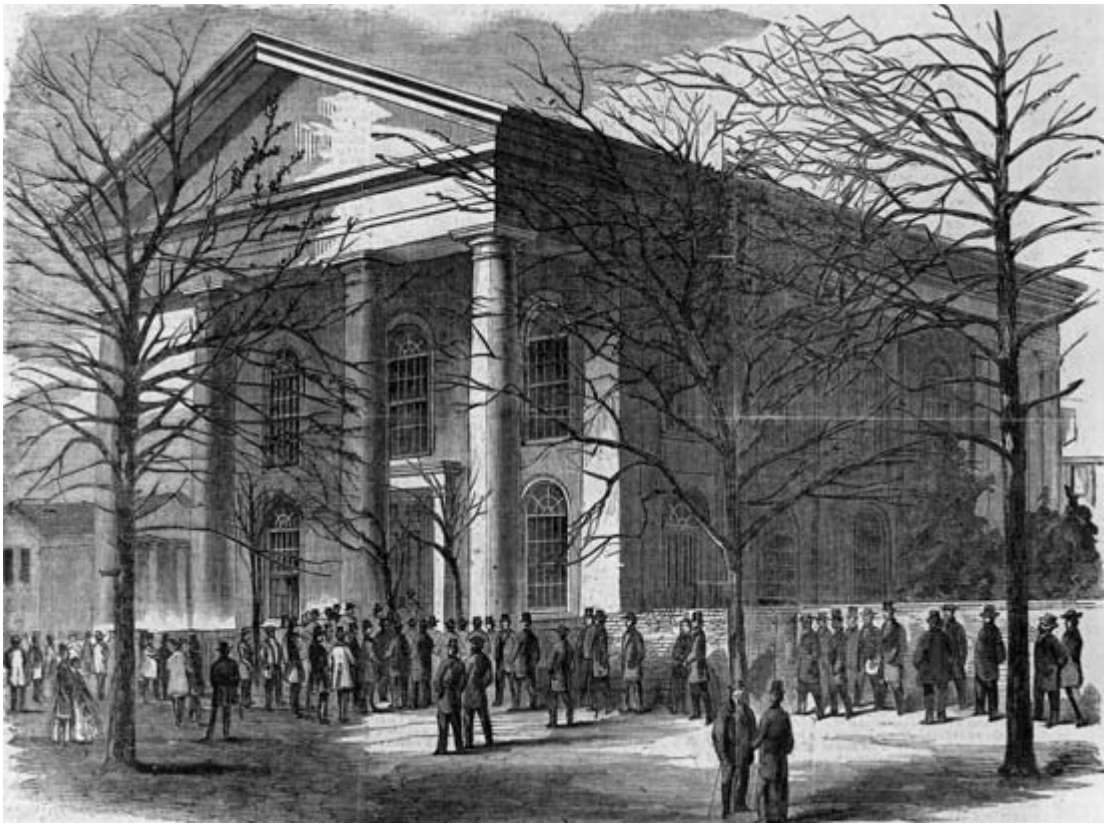
DIVIDEND GROWTH PORTFOLIO -- as of July 1, 2016 — Fundamental data as of July 1, 2016

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	3.27%	mid-Sep 2016	mid Sep 2016 (quart)	1.2	GOOD	GOOD	$58.00	6	1.19
Apple (AAPL)	2.28	2.38%	early Aug 2016	Aug 2016 (quart)	5.6	EXCELLENT	EXCELLENT	$148.00	7	0.65
Cisco (CSCO)	1.04	3.61%	early July 2016	early July 2016 (quart)	2.6	GOOD	EXCELLENT	$37.00	7	0.78
Coach (COH)	1.35	3.31%	early Sep 2016	early Sep 2016 (quart)	1.9	GOOD	GOOD	$41.00	3	0.99
Cracker Barrel (CBRL)	4.60	2.71%	mid July 2016	late July 2016 (quart)	1.7	GOOD	GOOD	$171.00	7	0.99
Energy Sector SPDR (XLE)	2.17	3.16%	late Sep 2016	early Sep 2016 (quart)	-	GOOD	NEUTRAL	-	UR	-
General Electric (GE)	0.92	2.92%	mid Sep 2016	Sep 2016 (quart)	3.1	EXCELLENT	GOOD	$32.00	6	0.98
Hasbro (HAS)	2.04	2.43%	late July 2016	mid Aug 2016 (quart)	1.6	GOOD	GOOD	$67.00	6	1.25
Intel (INTC)	1.04	3.18%	early Aug 2016	early Sep 2016 (quart)	2.3	GOOD	EXCELLENT	$38.00	3	0.86
Johnson & Johnson (JNJ)	3.20	2.64%	late Aug 2016	early Sep 2016 (quart)	2.7	GOOD	EXCELLENT	$121.00	7	1.00
Medtronic (MDT)	1.52	1.75%	early Jul 2016	Jul 2016 (quart)	1.6	GOOD	EXCELLENT	$71.00	7	1.23
Microsoft (MSFT)	1.44	2.81%	mid Aug 2016	mid Sep 2016 (quart)	2.7	GOOD	EXCELLENT	$52.00	4	0.98
Proctor & Gamble (PG)	2.68	3.16%	late July 2016	early Aug 2016 (quart)	1.5	GOOD	EXCELLENT	$70.00	6	1.21
PP&L (PPL)	1.52	4.04%	early Sep 2016	early Sep 2016 (quart)	Held for diversification reasons.			$33.00	6	1.14
Realty Income (O)	2.39	3.43%	monthly	monthly	2.0	GOOD	GOOD	$59.00	5	1.18
S&P Dividend ETF SPDR (SDY)	2.03	2.41%	mid Sep 2016	late Sep 2016	-	-	-	-	UR	-
Vanguard REIT ETF (VNQ)	3.31	3.73%	late Sep 2016	Sep 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.

Brexit: Secession Bells Are Ringing!

By Kris Rosemann and Brian Nelson, CFA



First Baptist Church in Columbia, S.C., where the first secession convention in the United States opened on Dec. 17, 1860. Source: Library of Congress, Washington, DC. Photo. Encyclopædia Britannica Online. Web. 24 Jun. 2016.

Market valuations remain stretched among stagnant global economic growth, and "Brexit" may be the catalyst for a correction.

In the paraphrased words of the well-known *The Day of the Jackal* author, Frederick Forsyth: the peasants have spoken. On June 23, the UK (EWU) held a referendum, in which anyone of voting age could take part, to decide whether the country should leave the European Union. The turnout was incredible at nearly 72%, and those voting to leave the union ("Leave") came in at 52% of the 30 million that cast a vote, setting the stage for "Brexit," or Britain's exit from the EU. On radio, Forsyth called the development the biggest uprising since the Peasants' Revolt in England in 1381. This is hardly the case of course, but global financial markets are plunging, and the financial sector (XLF, KBE) is getting shellacked as market participants try to figure out which banks may be left holding the bag.

We're still digesting the implications of "Brexit," but we're generally of the opinion that individual economic nuances of member nations of the European Union make centralized monetary policy and a common currency in the EU somewhat of an impediment to achieving individual sovereign-member macro goals. Unlike individual nations with distinct monetary and fiscal policies, the European Union is a combination of 28 member countries with generally unique economies and cultures with varying societal goals. Said differently, where the US can pursue both monetary and fiscal policy in tandem to achieve societal goals of price stability and full employment and the like, member nations of the EU are beholden to collective monetary policy that may at times fly in the face of what an individual sovereign may need at any given point in time. What is good for all may not be good for one. Critics point to this dynamic as to why a break-up of the EU may be an eventuality. Secession bells are ringing! Could Sweden and Denmark be next? What about France? Frexit?

Please see *Brexit...*on next page

***Brexit*...from previous page**

Though it's too early to know for sure whether "Brexit" may be a catalyst for a sustained global stock-market "correction" (beyond the plunge today), broader market valuations remain frothy, and global economic growth continues to stagnate. In the US, not only are valuations of S&P 500 companies stretched to ~17 times forward earnings, materially higher than both their 5-year and 10-year averages, but even some of the safest business models in the consumer staples sector (XLP), for example, are fetching valuations north of 20 times forward earnings. Though "Brexit" itself may not be enough to drive panic beyond today's knee-jerk reaction, within the context of an overheated and bubbly US stock market (DIA), it could very well be the tangible catalyst that sends the US market indices tumbling lower during the back half of 2016. Remember, the markets hate uncertainty, and this "Brexit" vote has only increased the market's uneasiness, which may be enough to keep new money on the sidelines. Without new money, equity markets will have trouble etching new highs.

There's more. Monetary policy in the US is something we're very mindful of, and "Brexit" may take any further hikes in the federal funds rate off the table, perhaps for the rest of 2016. Some of the "rate-hike" probability readings we've been witnessing suggest that not only are rate hikes probably off the table through at least November, there's now a possibility of the Fed actually cutting rates…at the next meeting (~6%). Can you believe it? Global capital is flocking to US Treasuries, driving the 10-year rate (TBT, TLT) under 1.5% at last check, approaching record lows of ~1.4% set in July 2012. Though lower rates are generally good for businesses and economic growth, the read-through in this case is that global markets are "scared," and the mighty US dollar (UUP) is one of the few places investors are willing to park cash (investors exchange foreign currency to US dollars--driving the price of the dollar higher relative to a basket of other currencies--to purchase Treasuries, which in turn then drives Treasury yields lower). The read through: market participants are "happy" with a paltry yield rather than taking on exposure to "risky" equities. Even a modest 20% correction following what has been one of the strongest runs in stock market history from the March 2009 panic bottom to the present day could be considered "normal." Please be aware of this.

In light of tumultuous conditions in the currency markets, which have sent the UK currency (pound) tumbling 10%+ to a 30-year low, we're also paying close attention to equities levered directly or indirectly to the USD-pound exchange rate (FXB). We would expect some spillover effects on multinationals, particularly those with significant revenue bases in the UK (pound) and parts of their cost structure overseas (in US dollars and other currencies), reflecting an inconvenient currency mismatch. Some companies with significant revenue exposure to the UK include Penske Auto (PAG), PPL (PPL), Xerox (XRX), Copart (CPRT) Molson Coors (TAP), Ford (F), and News Corp (NWSA), among others. US investors holding ADRs may feel the pinch from a weakening pound as well. Some equities that may fit this profile include AstraZeneca (AZN), BP (BP), Diageo (DEO), GlaxoSmithKline (GSK), Fiat Chrysler (FCAU), Pearson (PSO), Shire (SHPG), Smith & Nephew (SNN), and Unilver (UL, UN), among others. Income investors that are counting on UK-based equities that pay dividends in pounds may also see a cut in their paychecks.

Company (Ticker)	Share Price Drop[1]
Lloyds Banking Group (LYG)	-25.3%
The Royal Bank of Scotland (RBS)	-23.0%
Barclays PLC (BCS)	-22.2%
Deutsche Bank AG (DB)	-16.2%
UBS Group (UBS)	-12.9%
Morgan Stanley (MS)	-9.4%
Citigroup (C)	-8.0%
HSBC Holdings (HSBC)	-7.8%
Bank of America (BAC)	-6.8%
Goldman Sachs (GS)	-6.1%
JPMorgan Chase (JPM)	-5.2%
Wells Fargo (WFC)	-3.7%

1) As of intraday 6/24/16

Our team is monitoring the European banks closely. Barclays (BCS), Royal Bank of Scotland (RBS), Lloyds Banking (LYG), HSBC (HSBC), Deutsche Bank (DB), and UBS (UBS) were all down considerably, with Barclay's, RBS, and Lloyds giving back nearly 30% of their respective market values. Ongoing uncertainty about what may or may not constitute the European Union and any changes in the banking regulatory environment following Britain's exit from the EU may crimp lending causing a slowdown in loan growth and economic resiliency. Many view the UK as a springboard to further business in the European continent and a less-cohesive link between the UK and the EU could end up being quite disruptive, at least in the near term.

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Of particular concern, however, is that the massive move in the pound may expose banking equities to unforeseen credit and currency risks. We would not be surprised to hear of hedge fund failures that were rocked as a result of such currency moves. Market observers may remember the "fall out" of the now-defunct Long Term Capital Management, which failed as a result of bad currency bets. Such a concern is reverberating through the US-based global money centers: Citigroup (C), Bank of America (BAC), JP Morgan (JPM), Wells Fargo (WFC), Goldman Sachs (GS), and Morgan Stanley (MS) -- all down more than 5%. We continue to retain exposure to the US banking sector, however, as the stress tests, released June 23, continue to show a resilient financial foundation in the States. We're watching the yield curve closely, however.

"Brexit" is also expected to have an impact on the UK transportation industries. Early estimates are projecting UK air passenger volume to be down by 3%-5% by 2020, mostly due to the expectations for an economic downturn brought about by the collapse of the British pound. The UK air market is dominated by outbound traffic, and the weakening of the pound relative to other currencies will weigh on the demand of outbound travel. US airlines Delta (DAL) and United Continental (UAL) are among those impacted by reduced expectations for travel out of London and the UK, but American Airlines (AAL), which generates nearly 20% of total revenue from the Atlantic region that includes the UK, has been the biggest loser of the group thus far.

Global economic uncertainty and financial market turmoil means that its "gold bug" season, and many of the world's large gold miners are catching a bid on "Brexit" news. Newmont Mining (NEM), Barrick Gold (ABX), Yamana Gold (AUY), Gold Corp (GG), and Eldorado Gold (EGO), for example, are all bucking the sell-off June 24, as traders flock to the yellow metal for "safety." The SPDR Gold Shares ETF (GLD) is advancing ~5% today, but not all commodities are being spared. Dollar-denominated crude oil (USO) and copper prices are tumbling as concerns about global growth return to the fore, but the latter two have bounced considerably in the past several months. Big commodity producers BHP (BHP) and Rio Tinto (RIO) are feeling pain, both down more than 7%. The cost of protection is also on the rise, and on the basis of a time consideration to expiration, we think it's ripe to close out the June 30 put option position on the S&P 500 SPDR ETF (SPY) in both newsletter portfolios (at $1.19 per contract).

As for newsletter holdings, Altria (MO), the Utilities Sector SPDR (XLU) and Realty Income (O) continue to power higher amid the chaos. Our cash positions in the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio stand at ~15% and ~25%, respectively, as we wait patiently for the dust to settle. It's been quite the morning! Please let our team know if we can elaborate further.

Keep Calm and Carry On?

By Brian Nelson, CFA

Brexit may or may not be a big problem. Time will tell.

But what matters and eventually becomes its own catalyst, however, is valuation. The forward price-to-earnings multiple on S&P 500 companies (SPY) is currently ~16.5 times, above its 5-year (14.6) and 10-year averages (14.3). This is the real story. Assuming a reversion to the 10-year average multiple, for example, the S&P 500 can be considered "fairly valued" at $1,811, a drop of another 10% from ~2,000 levels. You don't need us to tell you that the markets have practically gone straight up the past seven years from the March 2009 panic bottom through today, with the S&P 500 effectively tripling since that fateful day. We haven't yet begun to see the froth come out of the US stock markets yet, and it's very important that readers understand that markets overshoot to the downside all the time.

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We're not worried. Our newsletter portfolios are positioned nicely. We hold rather lofty cash balances in both, approximately 15% in the Best Ideas Newsletter portfolio and approximately 30% (was 25%) in the Dividend Growth Newsletter portfolio. We love "dry powder," so when Mr. Market starts having a panic attack, we can increase exposure to areas that we like. The biggest challenge for investors seeking to put new money to work, however, is that most equities in the US have reached "bubble" proportions. You know this--we've been saying it for months. Consumer staples (XLP) equities are trading at nearly 21 times forward earnings, and cyclical equities, the consumer discretionary (XLY) sector and the industrials (XLI) sector, for example, are trading at peak multiples on cyclical peak earnings. Most market observers know that when investors are paying peak multiples on cyclical peak earnings, trouble may be around the corner.

Of course the markets are setting up for a nice shake out, but that's okay, and it's not because of Brexit. The market will always be a weighing machine, and valuation will always be the ballast that ties equity prices to intrinsic values over time. Those that forgot this recently may now be selling their positions aggressively. We're not doing anything. We love that two of our largest weightings in both newsletter portfolios, Altria (MO) and Johnson & Johnson (JNJ), continue to ratchet to new all-time highs! We love that the Utilities Select SPDR (XLU) continues to offset weakness in several holdings in the Best Ideas Newsletter portfolio. We love the resiliency of Realty Income (O). With every percentage point fall in the S&P 500, we add 15 basis points and 25 basis points of relative outperformance in the Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio, all else equal, respectively. Nobody likes it when the markets go down, but we run the newsletter portfolios to achieve the goals of them.

There will be some winners and there will be some losers, but we've been expecting a broad market sell-off even as we've added some incremental exposure to the newsletter portfolios recently -- in fact, we just closed our put option positions. We expect broader markets to continue to be choppy, and while we continue to expect alpha generation from both newsletter portfolios, we wanted to provide an incremental add-on feature that gives members more individual stock-selection options, outside of our coverage universe. This is why we launched our brand new publication, the Nelson Exclusive. I think it's a fantastic way to get more from Valuentum, while not blending the goals of newsletter portfolio management with individual standalone security selection, which are two different dynamics. What may be best for a newsletter portfolio may not be best on an individual basis. Though we can never provide personalized advice or recommendations, the Nelson Exclusive meets this need for members. You asked, we answered.

What a difference a couple weeks make. If Microsoft (MSFT) had just been a bit more patient, it probably wouldn't have leapt head-first into the LinkedIn (LNKD) deal following the Brexit news. Of course Microsoft is focusing on the long term, but focusing on the long term doesn't mean prudence should be thrown out the window. Microsoft significantly overpaid for LinkedIn as is, and it probably would have been able to save a couple billion dollars, given that LinkedIn's equity would have assuredly faced abnormal selling pressure in light of existing market conditions. This isn't about Monday morning quarter-backing or hindsight being 20-20, but it's more about common market sense. We're not sure what the board of Microsoft was thinking, and we're still comfortable with our decision to have removed half of its position in the Dividend Growth Newsletter portfolio. After all, if the board agreed to spend up for LinkedIn, what other mistakes could the board be making…right now?

We're paying the most attention to the equity market activity of the European banks (XLF, KBE). Our thesis on the banking sector is a unique one, but it's also tried-and-true. That the market values of Barclays (BCS), Royal Bank of Scotland (RBS), and Lloyds Banking (LYG) are dropping another 15%-20% on the trading session June 27 is flat-out significant, as their market capitalization is incredibly important when it comes to gauging counterparty, dealer and credit risk, not to mention their ability to raise incremental equity capital, should that be necessary. The global financial system operates on confidence, and when confidence is shattered for reasons that may be fair or not (real or perceived), the implications are far reaching. Those that experienced the Financial Crisis first-hand know that when it

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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 may be fully-invested at times, 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	Est. Div Yield	VBI	Div Growth	Div Cushion
Western Gas	WES	Energy	7.3%	6	EXCELLENT	1.7
Buckeye Partners	BPL	Energy	7.2%	6	GOOD	1.5
Holly Energy	HEP	Energy	6.8%	6	EXCELLENT	1.8
Enterprise Product Partners	EPD	Energy	6.5%	6	EXCELLENT	2.0
Iron Mountain	IRM	Industrials	5.9%	6	GOOD	1.5
Spectra Energy Partners	SEP	Energy	5.4%	7	EXCELLENT	1.8
Garmin	GRMN	Industrials	5.0%	6	GOOD	1.8
Magellan Midstream	MMP	Energy	4.8%	6	EXCELLENT	1.6
Entergy	ETR	Energy	4.4%	6	GOOD	1.4
QUALCOMM	QCOM	Information Technology	4.4%	6	EXCELLENT	3.5
Lexmark	LXK	Information Technology	4.2%	6	EXCELLENT	1.5
Caterpillar	CAT	Industrials	4.2%	6	GOOD	0.7
Retail Properties of America	RPAI	Financials	4.2%	7	EXCELLENT	1.3
Diebold	DBD	Industrials	4.1%	6	GOOD	1.8
ABB	ABB	Industrials	4.1%	6	GOOD	1.3
Philip Morris	PM	Consumer Staples	4.1%	6	GOOD	0.6
Guess	GES	Consumer Discretionary	4.1%	6	EXCELLENT	2.5
Cummins	CMI	Industrials	4.0%	6	EXCELLENT	2.0
Enbridge	ENB	Energy	4.0%	6	EXCELLENT	2.3
Hewlett-Packard	HPQ	Information Technology	4.0%	7	GOOD	2.1
Digital Realty Trust	DLR	Financials	4.0%	7	EXCELLENT	1.4
H&R Block	HRB	Consumer Discretionary	3.8%	6	GOOD	1.7
Cisco	CSCO	Information Technology	3.7%	7	EXCELLENT	2.6
AbbVie	ABBV	Health Care	3.6%	7	EXCELLENT	1.3
Emerson Electric	EMR	Industrials	3.6%	6	EXCELLENT	1.8
CA Tech	CA	Information Technology	3.5%	7	EXCELLENT	3.2
Altria Group	MO	Consumer Staples	3.5%	6	GOOD	1.2
Nu Skin	NUS	Consumer Discretionary	3.4%	7	EXCELLENT	2.7
IBM	IBM	Information Technology	3.4%	6	EXCELLENT	1.7
Reynolds American	RAI	Consumer Staples	3.3%	7	GOOD	0.5
Boeing	BA	Industrials	3.3%	7	EXCELLENT	2.0
Western Union	WU	Information Technology	3.3%	7	EXCELLENT	2.5
Thomson Reuters Corp	TRI	Financials	3.3%	7	GOOD	1.1
Merck	MRK	Health Care	3.3%	6	GOOD	1.9
American Eagle	AEO	Consumer Discretionary	3.3%	7	EXCELLENT	3.0
Procter & Gamble	PG	Consumer Staples	3.2%	6	EXCELLENT	1.5
United Parcel Service	UPS	Industrials	3.2%	7	EXCELLENT	1.6
Gap	GPS	Consumer Discretionary	3.1%	7	EXCELLENT	2.4
AVX Corp	AVX	Information Technology	3.0%	6	EXCELLENT	3.6
Unilever N.V.	UN	Consumer Staples	3.0%	6	GOOD	1.4
Archer-Daniels-Midland	ADM	Consumer Staples	3.0%	7	EXCELLENT	2.4
General Electric	GE	Industrials	3.0%	6	GOOD	3.1
Unilever PLC	UL	Consumer Staples	3.0%	6	GOOD	1.4
Darden Restaurants	DRI	Consumer Discretionary	2.9%	7	GOOD	1.5
Xerox	XRX	Industrials	2.9%	9	EXCELLENT	2.1
Deere	DE	Industrials	2.8%	6	EXCELLENT	1.4
Genuine Parts	GPC	Consumer Discretionary	2.8%	6	EXCELLENT	1.6
Kimberly-Clark	KMB	Consumer Staples	2.8%	7	GOOD	1.2
Waste Management	WM	Industrials	2.8%	7	GOOD	1.6
Johnson & Johnson	JNJ	Consumer Staples	2.8%	7	EXCELLENT	2.7
Eli Lilly	LLY	Health Care	2.7%	6	GOOD	2.0
Cracker Barrel	CBRL	Consumer Discretionary	2.7%	7	GOOD	1.7

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

The Strongest Dividend Payers Yielding Over 2%

By Valuentum Analysts

There are a number of ways to evaluate the health of a company's dividend. We think a minimum threshold for a company's yield is par for the course in any income-oriented screen, and we peg the dividend yield hurdle rate for this screen at 2%. For firms that make this cut, we want to find those that generate free cash flow at a pace that is far larger than the cash paid out as dividends and have a strong balance sheet to boot, or companies that have high Dividend Cushion ratios.

Enter stocks that have the highest multiplicative combination of their dividend yield and Dividend Cushion ratio. We exclude the business models of master limited partnerships and real estate investment trusts in this screen and focus exclusively on corporates. Income investors have a lot to choose from, and this screen is one of our favorites.

Company Name	Symbol	Sector	Est. Div Yield	Div Cushion	Multiplier
DeVry	DV	Consumer Discretionary	1.9%	8.5	15.76
QUALCOMM	QCOM	Information Technology	4.4%	3.5	15.47
GameStop	GME	Consumer Discretionary	5.8%	2.5	14.37
Automatic Data Processing	ADP	Information Technology	2.4%	5.5	13.10
Cooper Tire & Rubber	CTB	Consumer Discretionary	1.2%	10.6	12.22
MKS Instruments	MKSI	Information Technology	1.9%	6.3	11.93
Best Buy	BBY	Consumer Discretionary	3.7%	3.2	11.82
Abercrombie & Fitch	ANF	Consumer Discretionary	4.0%	2.9	11.48
CA Tech	CA	Information Technology	3.5%	3.2	11.08
AVX Corp	AVX	Information Technology	3.0%	3.6	10.99
Teva Pharma	TEVA	Health Care	2.5%	4.2	10.64
Apple	AAPL	Information Technology	1.9%	5.6	10.53
Graham Holdings Co	GHC	Consumer Discretionary	1.0%	10.4	10.39
Insperity	NSP	Information Technology	1.7%	5.9	10.14
Finish Line	FINL	Consumer Discretionary	2.2%	4.7	10.13
Intersil	ISIL	Information Technology	3.9%	2.6	10.09
Guess	GES	Consumer Discretionary	4.1%	2.5	9.97
American Eagle	AEO	Consumer Discretionary	3.3%	3.0	9.78
Cisco	CSCO	Information Technology	3.7%	2.6	9.62
Taiwan Semiconductor	TSM	Information Technology	3.3%	2.9	9.42
Fluor	FLR	Industrials	1.6%	5.7	9.32
Nu Skin	NUS	Consumer Discretionary	3.4%	2.7	9.29
General Electric	GE	Industrials	3.0%	3.1	9.17
Applied Materials	AMAT	Information Technology	2.0%	4.6	9.05
Garmin	GRMN	Industrials	5.0%	1.8	8.86
Superior	SUP	Consumer Discretionary	3.9%	2.2	8.74
Computer Sciences	CSC	Information Technology	1.7%	5.0	8.70
Resources Connection	RECN	Information Technology	2.6%	3.3	8.62
Western Union	WU	Information Technology	3.3%	2.5	8.43
Hewlett-Packard	HPQ	Information Technology	4.0%	2.1	8.40
Granite Construction	GVA	Industrials	1.2%	6.9	8.26
Oracle	ORCL	Information Technology	1.7%	5.0	8.24
Intel	INTC	Information Technology	3.6%	2.3	8.23
Methode Electronics	MEI	Information Technology	1.2%	6.6	8.19
Paychex	PAYX	Information Technology	3.1%	2.6	8.18
Nvidia	NVDA	Information Technology	1.6%	5.2	8.17
CTS Corp	CTS	Information Technology	0.9%	9.2	8.02
STMicroelectronics	STM	Information Technology	6.9%	1.2	8.00
Chico's FAS	CHS	Consumer Discretionary	2.5%	3.2	7.96
Cummins	CMI	Industrials	4.0%	2.0	7.93
Chicago Rivet	CVR	Consumer Discretionary	3.0%	2.6	7.81
Computer Prog and Syst	CPSI	Health Care	5.0%	1.6	7.76
Lear Corp	LEA	Consumer Discretionary	1.0%	8.0	7.69
Microsoft	MSFT	Information Technology	2.9%	2.7	7.65
Xilinx	XLNX	Information Technology	2.5%	3.1	7.61
Gentex	GNTX	Consumer Discretionary	2.5%	3.0	7.56
Scholastic Corp	SCHL	Consumer Discretionary	1.7%	4.4	7.55
Power Integrations Inc	POWI	Information Technology	1.1%	6.8	7.51
Meridian	VIVO	Health Care	4.2%	1.8	7.48
Williams-Sonoma	WSM	Consumer Discretionary	2.8%	2.6	7.40

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
Peabody Energy	BTU	Industrial Minerals	0.2%	VERY POOR	-355.4
CONSOL Energy	CNX	Industrial Minerals	0.5%	VERY POOR	-113.5
KB Home	KBH	Homebuilders	0.7%	VERY POOR	-50.1
Windstream	WIN	Telecom Services - diversified	6.9%	VERY POOR	-36.1
Lennar	LEN	Homebuilders	0.3%	VERY POOR	-27.6
Devon Energy	DVN	Independent Oil & Gas	0.7%	VERY POOR	-24.2
Anadarko	APC	Independent Oil & Gas	0.4%	VERY POOR	-22.1
D. R. Horton	DHI	Homebuilders	1.1%	VERY POOR	-10.1
Ryder System	R	Rental and Leasing	2.5%	VERY POOR	-8.5
Hess	HES	Refiners	2.3%	VERY POOR	-8.1
Yamana Gold	AUY	Metals & Mining - gold	0.4%	VERY POOR	-6.6
Tailored Brands	TLRD	Retail - Men's, Women's Apparel	4.2%	VERY POOR	-6.6
TAL Intl	TAL	Rental and Leasing	13.1%	VERY POOR	-5.5
Allegheny Technologies	ATI	Aluminum	2.6%	VERY POOR	-5.4
Barrick Gold	ABX	Metals & Mining - gold	0.4%	VERY POOR	-4.3
ConocoPhillips	COP	Major Oil & Gas	2.4%	VERY POOR	-4.0
MDC	MDC	Homebuilders	4.2%	VERY POOR	-3.9
Textainer	TGH	Rental and Leasing	8.7%	VERY POOR	-3.6
Murphy Oil	MUR	Refiners	7.3%	VERY POOR	-3.5
Cablevision	CVC	Media - CATV	1.8%	VERY POOR	-3.3
NiSource	NI	Utilities	3.0%	VERY POOR	-3.3
Noble Energy	NBL	Independent Oil & Gas	1.1%	VERY POOR	-3.3
Apache	APA	Independent Oil & Gas	1.9%	VERY POOR	-3.2
Olin Corp	OLN	Chemicals - mid/small	3.5%	VERY POOR	-2.7
PetroChina	PTR	Major Oil & Gas	2.1%	VERY POOR	-2.6
Wendy's Co	WEN	Restaurants - Fast Food & Coffee	2.4%	VERY POOR	-2.5
Deltic Timber	DEL	Building Materials	0.6%	VERY POOR	-2.2
Huntsman	HUN	Chemicals - broad	3.3%	VERY POOR	-2.1
CF Industries	CF	Chemicals - agriculture	4.7%	VERY POOR	-2.0
Quad/Graphics Inc	QUAD	Book Publishing	9.4%	VERY POOR	-1.9
Rent-A-Center	RCII	Rental and Leasing	2.6%	VERY POOR	-1.9
Service Corp Intl	SCI	Personal Services	2.0%	VERY POOR	-1.8
Royal Caribbean	RCL	Leisure	1.8%	VERY POOR	-1.7
Natural Resource Partners	NRP	Industrial Minerals	15.5%	VERY POOR	-1.7
Time Warner Cable	TWC	Media - CATV	1.5%	VERY POOR	-1.7
Alcoa	AA	Aluminum	1.3%	VERY POOR	-1.6
Centurylink	CTL	Telecom Services - diversified	6.9%	VERY POOR	-1.6
Silgan	SLGN	Containers & Packaging	1.2%	VERY POOR	-1.6

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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comes to banking perception is reality, and if market participants start to think the European banks are in trouble, the very activity by such market participants (selling their equity, reducing exposures, calling in positions, etc) will make it so.

From our ETF report on the Banks & Financials Services sector:

The Banking Industry Is All About Confidence

> The financial sector, and the underlying banking industry in particular, is distinctly different than most other sectors like industrials, retail, or healthcare, for example. Unlike the latter industries, banks use money to make money (net interest income), instead of using operating assets like property, plant and equipment (PPE) and raw materials to drive revenue and resulting free cash flow. This means that continued access to money and credit is the primary source of banks' economic returns and more specifically their survival.
>
> The "5 Cs of credit" — character, capacity, capital, collateral, and conditions — is a widely-followed framework and generally-accepted guideline for lending to consumers, but for corporate entities, we think another C is much more important: confidence. In almost every situation where a bank has encountered trouble, it has resulted from a loss of confidence in the sustainability of the entity as a going concern. The loss of confidence could originate from counterparties, intermediaries, depositors or clients, or from any other core stakeholder. Lack of confidence typically spreads quickly.
>
> Lehman Brothers' bankruptcy filing in 2008, for example, was accelerated by clients leaving the firm and credit rating downgrades that completely obliterated market confidence in the sustainability of the entity. Barclays now owns Lehman, which had been a staple in American society since its founding in 1850. Washington Mutual had its foundation rocked that same year when its customers, over a period of just 9 days, withdrew ~$17 billion in deposits, or about 10% of its total deposits, in the modern-day equivalent of a bank run. The Federal Deposit Insurance Corporation seized Washington Mutual and sold the 120-year-old company to JP Morgan (JPM) shortly thereafter. In both cases, the loss of confidence prompted disaster, leaving shareholders with only a fraction of their invested capital.
>
> Quite simply, if the market does not have confidence in a banking entity, that banking entity will cease to exist. Though other business models such as master limited partnerships and real estate investment trusts depend on continuous access to the credit markets and incremental capital, a run-on the-bank dynamic is a risk that is almost entirely unique to banks. FDIC insurance does not cover the financial products that a bank offers, including stocks, bonds, mutual funds, and life insurance, and the standard FDIC insurance amount is $250,000 per depositor, per insured bank. Because the government cannot insure everything and plan for all risks, traditional run-on the bank dynamics can never be completely hedged away, no matter how advanced or regulated the banking system becomes.
>
> An insufficient capital position brought about by excessive risk-taking (leverage), poor lending standards, and under-water loans as a result of asset declines may be more tangible operating reasons for a bank's failure, but without confidence, even strong banks cannot survive.
>
> **The Financial Crisis of 2008 and the Great Recession**
>
> During the past three decades alone, there have been three significant banking crises: the savings and loan crisis of the late 1980s/early 1990s; the fall of Long Term Capital Management and the Russian/Asian financial crisis of the late 1990s; and the Great Recession of the last decade that not only toppled Lehman Brothers, Bear Stearns, Washington Mutual, and Wachovia but also caused the seizure of Indy Mac, Fannie Mae and Freddie Mac.

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> We believe that an investment in a bank must come with the acknowledgement of the distinct possibility that another financial crisis may occur at an unknown time in the future. The primary reason for this view rests on the fact that banks do not keep a 100% reserve against deposits. Our good friend George Bailey, played by actor Jimmy Stewart, in the movie It's a Wonderful Life knew this very well when he tried to discourage Bedford Falls residents from making a "run" on the famous and beloved Building and Loan. It's a movie that some of us have watched a dozen times or never at all, but it's a scene that's unforgettable.
>
> Washington Mutual fell prey to this very dynamic in 2008.
>
> In the testimony of Mr. JP Morgan before the Pujo Committee of 1912-1913, character is the only thing that matters in banking—or said differently, perceived confidence that the banking system will continue to work is really the duct tape that holds the financial markets together. Once this perceived confidence breaks down as it has many a time before, a "run on the bank dynamic" occurs. Stakeholders can't get their money fast enough. Such a unique risk will always be present for banking-firm investors relative to investors in general operating corporations.

What to expect from us in the coming days? It's important that you know that we're not in any rush to do much of anything in the newsletter portfolios. We may look to add to the position in Priceline.com (PCLN), which has experienced considerable selling pressure in light of the expected decline in air travel in Europe and across the Atlantic from Brexit, but we're still watching shares. We'll be removing the position in Talen (TLN) from the Dividend Growth Newsletter portfolio in coming days – the spin-off of PPL Corp (PPL) was bought out recently, and we now have cleaned out the position in this July edition of the Dividend Growth Newsletter portfolio, July 1. We're only a few percentage points from all-time highs in the S&P 500. It's still too early for bargain hunting, in our view. We could be in store for much more selling. Keep calm and carry on!

Yum!: Does One Plus One Equal More Than Two?

By Valuentum Analysts

Image Source: Dave Proffer

Yum! Brands (YUM) has a fantastic portfolio of restaurants including KFC, Taco Bell, and Pizza Hut. It operates in more than 140 countries with nearly 43,000 restaurants, and despite the maturity of its three core concepts in the US, Yum! Brands continues to expand its store base at an incredible rate, particularly in Asia (in 2015 alone, it opened almost 2,400 new restaurants companywide, averaging ~6 new restaurants daily).

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Yum! Brands will be pursuing major changes in the near term, however, and is set to split into two publicly-traded, independent companies by the end of 2016: 'Yum! China' and 'Yum! Brands.' Though management says the split is "a classic example of 'one plus one equaling more than two' as it will enable each company to realize its full potential and achieve greater value on a standalone basis," we have to ask if this is true; wouldn't two strong structures working together cause better results than each of them working independently? Will the benefits truly outweigh the incremental challenges that will undoubtedly come from needing two of everything (two back offices, two executive teams and the like)?

First, let's address the brand new Yum! China. The company's 'China Division' continues to face ongoing challenges (distractions) from bird flu scares to poultry scandals (with system sales and same-store sales advancing only modestly and declining 4%, respectively, during fiscal 2015), and we would expect the spin-off of Yum! Brands' China operations into 'Yum! China' to allow for a distinct, new management team to take the reins and refocus on driving sourcing and supply-chain improvement without having the burden of catering to a broader geographical presence. The spin-off of the China business will also give Yum! China improved national appeal in the country, in our opinion, perhaps helping to better tie it to the daily eating habits of Chinese consumers, translating into further unit growth potential in the country's rising consumer economy (maybe even beyond existing robust expectations). But just how big can Yum! China become?

The executive team at Yum! China believes that its restaurant saturation point in China is an incredible 20,000 restaurants, nearly triple its current exposure of 6,900, which by itself makes it the largest quick-service player in the country (KFC continues to be a big favorite among Chinese consumers). We continue to be enamored by Yum! China's tremendous opportunity in China, and we believe its business model speaks of sustained growth given its long historical track record of successful unit expansion. Spun-off without the financial burden of any substantial debt, the soon-to-be publicly-traded Yum! China will be able to fund all of its capital needs (unit growth) from robust free cash flow generation. We're anxiously awaiting separate audited information, but we absolutely love this particular aspect of its business. Frankly, it's very hard not to like a balance-sheet cash-rich and free-cash-flow generating powerhouse, with incredible future growth prospects.

An investment in the soon-to-be spun off Yum! China, however, is not a complete no-brainer. For one, the company will retain all of the operating risk of running the restaurants, and unfortunately, the more recent past has shown that operating troubles in China can have profound implications on same-store sales performance, even as we say that its brand has bounced back from every pitfall thus far. The company will pad Yum! Brands' pockets with a nice franchise fee, and we can't say that the ever-changing Chinese regulatory environment will play to the company's favor. As the new executive team seeks to triple the number of restaurants in China in coming years, we'll be monitoring the tremendous execution risk associated with such a bold endeavor. Should same-store sales performance disappoint, or if economic malaise takes hold in the country, the growth runway could shorten, at least in the near term.

Now about Yum! Brands, its legacy business. For starters, "Yum! Brands' (also referred to as 'New Yum!') will remain a strong global company, but its financial risk will be significantly heightened as a result of the executive team's capital deployment ambitions. As with Yum! China, we believe a laser-focused executive team, now free of the time and effort that comes with making strategic decisions in China, will be able to shift its attention to other ways of improving its already strong restaurant concepts. Quite the savvy move and to establish Yum! Brands as an eventual "pure play" franchisor, it will be the beneficiary of a fixed franchise fee of 3% of system sales for KFC and Pizza Hut (and Taco Bell) from Yum! China. The stable but growing nature of the relationship between Yum! Brands and Yum! China will serve to provide a nice growing free cash flow stream to the former without it taking on any of the operational risks of running those units in China.

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But not all is a slam-dunk at legacy Yum! Brands either. The company, stripped of its presence in China, will now act as a leveraged, franchisor with a focus primarily on returning capital to shareholders. This sounds great, particularly for income investors, but is the executive team stretching too far to please? Moody's has proposed to assign Yum! Brands' credit to junk status (Ba1) in light of its leverage, something that we're surprised Yum! Brands is willing to accept, given its rather prudent nature of the past (the company has a corporate family rating of Ba3). With the combined, pre-spin-off entity holding a net debt position of $3+ billion at the end of 2015, the financial health of Yum! Brands will only become more leveraged in time (in fact, management is targeting a post-spin off leverage mark of ~5 times, which we feel is way too high, even for a tried-and-true franchisor). Management doesn't seem worried and plans to return ~$6.2 billion of capital to shareholders (mostly through buybacks) preceding the separation.

Though we believe the unit growth prospects of a debt-free Yum! China are truly fantastic, the competitive environment in the US may prove to be more difficult for legacy Yum! Brands to navigate to drive organic expansion. Competition from other restaurant concepts in the US will continue to pressure domestic growth at Yum! Brands, particularly from companies such as privately-held Chick-fil-A and the much-maligned Chipotle (CMG), which despite its recent norovirus troubles, is still a powerhouse within the Mexican food restaurant vertical. Innovations at Yum! Brands have helped combat some of the steps by its rivals, and we point to Taco Bell offering a wider breakfast selection, KFC offering its '$5 fill up,' and new chicken sandwich restaurant concept, Super Chix, which is similar in menu options as Chick-fil-A, as reasons to remain optimistic about Yum! Brands competitive profile in the US. We believe same-store sales performance at Yum! Brands will be critical for investors to watch post-transaction.

Let's dig into some of the expectations for fiscal 2017 for each soon-to-be separated company. Yum! China believes that it has the "capacity to support substantial same-store sales growth," and its strategy to retain its premier status in China remains unchanged. Investors should expect 15% growth in earnings per share per annum, but there are a lot of moving parts, operationally, that could cause rather large deviations from that target. We saw this on display during the past few years with bird flu scares and poultry scandals, which sent same-store sales in China tumbling significantly for months before recovering. Earnings were not spared the pain either, and we don't think an investment in Yum! China is for those with weak stomachs. Operating performance at Yum! China will have its ups and downs, more so than most.

Yum! Brands' is targeting a combination of ~15% of earnings per share growth plus its dividend yield, and we note that it will likely fit the profile of a steadily-growing income payer. Though too early to say, Yum! Brands may fetch a dividend yield in the ballpark of ~5%, much like that of overleveraged, franchisor peer, DineEquity (DIN), which runs a 99% franchised model of two powerhouse brands, Applebee's and IHOP – it, too, is significantly leveraged. Yum! Brands' free-cash-rich business model, which it expects to be 96% franchised by the end of 2017, should be able to cover its future dividend payments, though we'll have to get a better feel for its deleveraging targets to say for certain whether competing priorities for free cash won't drown it out over time. At the moment, management is targeting a sustained leverage ratio of 5x for Yum! Brands, which implies to us it will be holding that outsize level for some time, even into recessionary conditions.

Investors will soon have a couple choices with respect to Yum!: the debt-free, free-cash flow rich growth story of Yum! China, or the shareholder-friendly, overleveraged, capital-light, "pure-play" franchisor in Yum! Brands. Both investment ideas have strengths and weaknesses, and depending on the investor's goals and risk tolerances, either one could make sense, at the right price of course. We may not agree with management that one plus one will equal more than two, but we understand the pressures the board had in providing more options to all types of investors: growth, income and beyond. We understand the motivation behind the break up, and Yum! China and Yum! Brands will be fantastic entities in their own right. To each their own, as they say. The separation is expected to be completed by the end of 2016.

Walmart Forms Alliance with Leading Chinese E-commerce Firm

By Kris Rosemann

As some US corporations are finding the Chinese market an increasingly difficult one in which to operate, "China (May 2016)," Walmart (WMT) is taking moves to strengthen its presence in the world's second largest economy. On June 20, the retailing behemoth announced that it has entered into a partnership with JD.com (JD), one of China's largest e-commerce companies, a move that will enhance offerings to consumers throughout China via a combination of JD.com's e-commerce prowess and Walmart's traditional retail operations. While Walmart continues to expand internationally, Target (TGT) continues to retreat from non-US markets, even having abandoning efforts in Canada recently.

In the deal with JD.com, Walmart has agreed to sell its grocery-focused, Chinese e-commerce business Yihaodian to JD.com for a 5% stake in JD.com, worth ~$1.5 billion. JD.com will control the Yihaodian website while Walmart will continue to operate Yihaodian's direct sales business. Walmart will also continue to sell on the Yihaodian marketplace, which is expected to significantly improve JD.com's presence in eastern and southern China. JD.com will then receive the right of use to a wide variety of items from Walmart it previously did not have. The two firms will also cooperate to leverage their massive supply chains to increase the offerings for consumers across China, particularly through the expansion of the range of imported products sold.

Perhaps the most important aspect of the transaction is Walmart's gain of access to such a significant e-commerce platform and same-day delivery network in the second-largest (and still a fast growing) economy in the world. JD.com's warehouse and delivery network covers approximately 600 million consumers. The American retail giant has had a difficult time in China--it operates just over 400 stores in the country despite having a presence there for ~20 years--and bolstering its online presence may just be the key to future success, particularly when considering that categories such as groceries and household goods have become more prominent items for online shoppers in China as of late. Walmart's Sam's Club operations figure to be a beneficiary of such a dynamic, too. The first Sam's Club was opened in 1996 in China.

Walmart believes the deal has the potential to greatly impact its online traffic from JD.com's large customer base and delivery network. Walmart's Yihaodian owns and operates ~250 delivery and pickup stations across China, while JD.com boasts nearly 6,000 of such hubs. Prior to the deal, Walmart had just over 1.5% of the total Chinese online market, good for number 6 overall in the country, a far cry from JD.com's ~20% share of the Chinese e-commerce marketplace. Righting the ship in China has the potential to be a material driver for Walmart's growth in coming years; the firm has meaningful potential to grow its presence in the country, both in terms of e-commerce and physical store count. The partnership with JD.com also has serious potential to aid in Walmart's online initiative, something its ownership of Yihaodian did little to shore up as e-commerce sales growth across the globe has decelerated in recent quarters at Walmart.

Though shares of JD.com have caught an updraft as a result of the deal, this transaction is more about the potential for an additional growth driver for Walmart, in our opinion. Walmart gains ~$1.5 billion in shares of JD.com that are currently trading at a material discount to our fair value estimate of $32, as well as meaningful potential to grow its presence in the largest online marketplace in the world. International expansion, particularly in Brazil and China, has been a focus at Walmart, and this transaction could be a very nice catalyst for more non-US growth initiatives. Though there may be upside for shares of JD.com on the basis of our fair value estimate, we note, however, the firm is still exposed to risks associated with the uncertainties in the Chinese economy and its ever-changing regulatory environment (and it has yet to demonstrate that it can sustainably turn a profit). The deal, however, may still turn out to be a large positive for JD.com as it relates to its competitiveness with the likes of Alibaba (BABA), which owns nearly half of e-commerce share in the country.

Quick Update: Starbucks -- What a Company

By Jessica Bishop

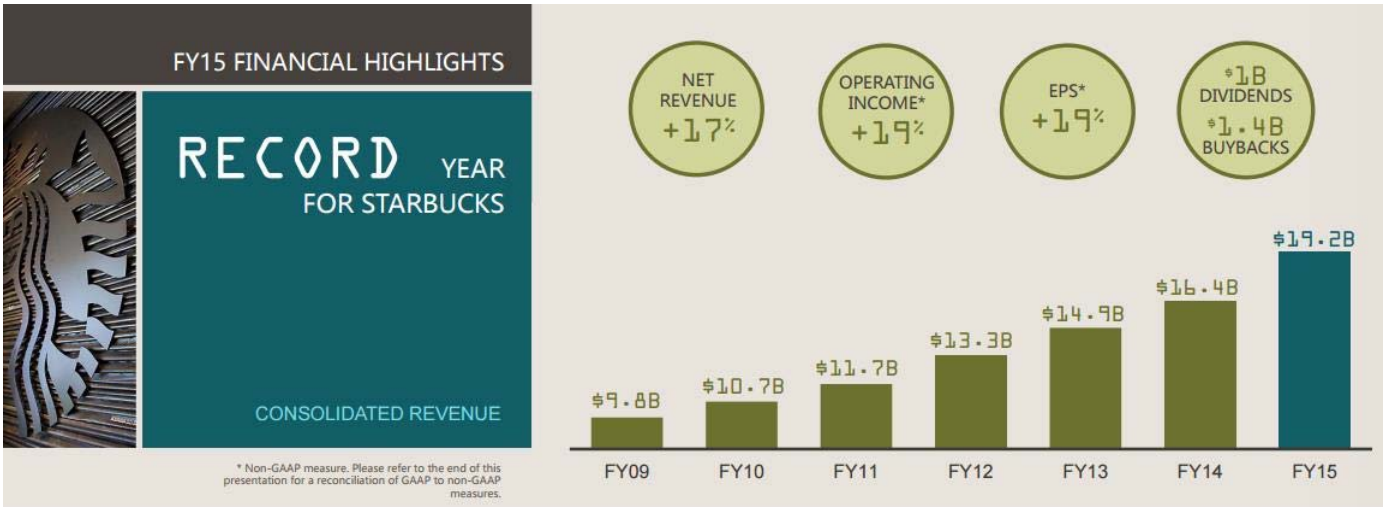

Image Source: Starbuck's 2016 Annual Meeting of Shareholders

With coffee being an integral part of so many people's daily routine, Starbucks (SBUX) has captured the hearts of coffee drinkers everywhere and has become the face of upscale, high-end coffee with its tremendous brand recognition. Along with its brand comes its unmatched loyalty program, as people just can't seem to get enough of Starbucks. It has taken great strides toward mobile advancements such as My Starbucks Rewards (MSR) that has gained more than 10 million active members (grew 28% in fiscal 2015 from fiscal 2014) in the US with card loads in North America alone at $5+ billion in fiscal 2015. The strength of its loyal customer base has allowed the firm to increase its comparable same-store sales 7% and open 1,677 new stores across the globe in fiscal 2015. With 23,000+ stores already in place, Starbucks has shifted its focus from domestic store count growth to expanding internationally (mostly in China and Japan with China being the largest market outside of the US); 70% of its ~1,800 new stores in fiscal 2016 opened outside of the US.

Starbucks' brand strength also allows it to increase its prices while still retaining the vast majority of its customers. Not only are the prices of its products comparatively higher than rivals, but so is its share price, as it is trading at a full valuation, both in terms of our fair value estimate and relative valuation. Based on our future forecasts, the company's forward P/E is ~29, significantly higher than our estimate of its peer median of ~22.1 Competition from Dunkin' Donuts (DNKN) may increase pressure as it works to pull marginally more value-conscious customers from Starbucks. For example, Dunkin' offers lower prices such as its 'Happy Hour' of $0.99 any size iced coffee. We also note that Starbucks' margin performance is in part tied to the cost of coffee, such as the price of Arabica coffee beans, which can be volatile and can be impacted by a variety of factors. Though with a company like Starbucks, it would take a substantial price fluctuation in its input costs to materially affect its financial strength. Starbucks has a net debt position of $700+ million as of the end of fiscal 2015 on the balance sheet, but with free cash flow generation of ~$2.45 billion in the year, we aren't too worried about its financial health.

The potential to sell products such as coffee blends in grocery stores has risen, offering Starbucks the potential to tap into the market of consumers who primarily drink coffee outside of the coffee shop. The firm has done well in targeting this group as of late, as it has ~500 signature aisles in grocery stores and has become a top provider in the 'Premium Roast and Ground' space as well as a major provider of K-cups. This 'CPG, Foodservice and Other' segment generated ~$2 billion in sales in fiscal 2015, more than 10% of the total revenue of the company. Its acquisition of Teavana has also helped drive revenue growth, as it continues to generate large sales in US stores ($1 billion fiscal 2015, up 12% from the prior year). It has only just started to introduce its tea line to China and other international countries.

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Though it may be easy to conclude that this acquisition will be a major driver of sales in the Chinese market, cultural differences may cause differences in preferences of customers. We're monitoring developments closely.

Starbucks continues its consistent year-over-year revenue growth, as it has achieved a record $19.2 billion in fiscal 2015 from $13.3 billion in fiscal 2012, representing a 13% compound annual growth rate (CAGR). The company has also experienced excellent annual growth in operating cash flow, as it has grown to over $3.7 billion in fiscal 2015 from $1.8 billion in fiscal 2012, a 29% CAGR. This strong operating cash flow growth has led to improved free cash flow generation; the firm reported ~$2.45 billion in fiscal 2015, compared to approximately -$550 million (negative ~$550 million) in fiscal 2014, mostly due to litigation charges over a dispute with Kraft (KHC). Since such charges are not recurring, we expect free cash flow generation to remain positive moving forward.

What a fantastic company Starbucks is, but investors are paying up for its earnings, just as consumers are paying up for its coffee. Many are betting Starbucks will grow into its lofty valuation, however, and it may very well do so (it has done so before). Savvy value investors may look for more of a meaningful pullback before considering shares in their portfolios, and that's where we feel most comfortable. Shares yield ~1.5%.

Financial Information (in millions, except per share data):

As of and for the Fiscal Year Ended [1]	Sep 27, 2015 (52 Wks)	Sep 28, 2014 (52 Wks)	Sep 29, 2013 (52 Wks)	Sep 30, 2012 (52 Wks)	Oct 2, 2011 (52 Wks)
Results of Operations					
Net revenues:					
Company-operated stores	$ 15,197.3	$ 12,977.9	$ 11,793.2	$ 10,534.5	$ 9,632.4
Licensed stores	1,861.9	1,588.6	1,360.5	1,210.3	1,007.5
CPG, foodservice and other	2,103.5	1,881.3	1,713.1	1,532.0	1,060.5
Total net revenues	$ 19,162.7	$ 16,447.8	$ 14,866.8	$ 13,276.8	$ 11,700.4
Operating income/(loss)[2]	$ 3,601.0	$ 3,081.1	$ (325.4)	$ 1,997.4	$ 1,728.5
Net earnings including noncontrolling interests[2]	2,759.3	2,067.7	8.8	1,384.7	1,248.0
Net earnings attributable to noncontrolling interests	1.9	(0.4)	0.5	0.9	2.3
Net earnings attributable to Starbucks[2]	2,757.4	2,068.1	8.3	1,383.8	1,245.7
EPS — diluted[2]	1.82	1.35	0.01	0.90	0.81
Cash dividends declared per share	0.680	0.550	0.445	0.360	0.280
Net cash provided by operating activities	3,749.1	607.8	2,908.3	1,750.3	1,612.4
Capital expenditures (additions to property, plant and equipment)	1,303.7	1,160.9	1,151.2	856.2	531.9
Balance Sheet					
Total assets	$ 12,446.1	$ 10,752.9	$ 11,516.7	$ 8,219.2	$ 7,360.4
Long-term debt (including current portion)	2,347.5	2,048.3	1,299.4	549.6	549.5
Shareholders' equity	5,818.0	5,272.0	4,480.2	5,109.0	4,384.9

(1) Our fiscal year ends on the Sunday closest to September 30.

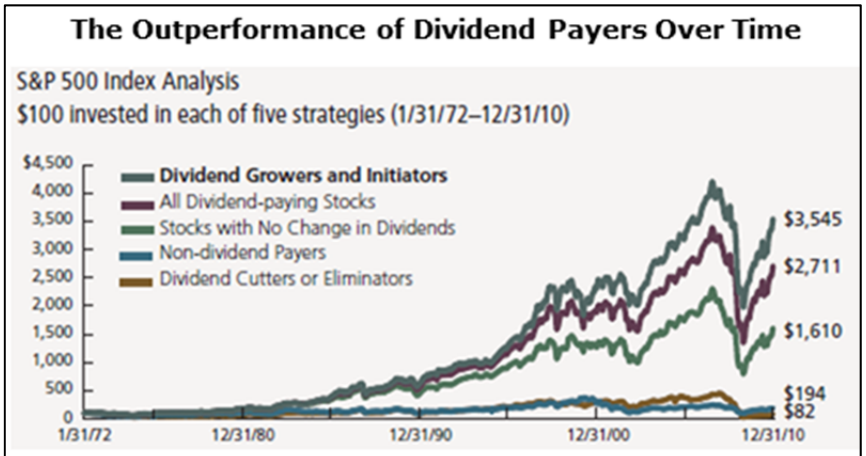
(2) Fiscal 2013 results include a pretax charge of $2,784.1 million resulting from the conclusion of our arbitration with Kraft Foods Global, Inc. The impact of this charge to net earnings attributable to Starbucks and diluted EPS, net of the related tax benefit, was $1,713.1 million and $1.12 per share, respectively.

Image Source: Starbuck's 2015 10-K

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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About Our Valuentum Dividend Cushion…**from previous page**

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 1Indicates 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 beyond last reported year.

Backtesting Methodology: Net balance sheet (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.

Please see *About Our Valuentum Dividend Cushion…*on next page

*About Our Valuentum Dividend Cushion...*from previous page

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

Valuentum Dividend Growth Newsletter: Volume 5, Issue 7

Valuentum's Dividend Growth Newsletter is published monthly. To receive this newsletter on a monthly basis, please subscribe to Valuentum by visiting our website at http://www.valuentum.com. Or contact us at info@valuentum.com.

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).

Image Links:

Page 14: https://www.flickr.com/photos/deepphoto/3019206369/in/photolist-5ANdSe-nfpGfN

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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