OUR DIVIDEND GROWTH NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

November 1, 2016
Volume 5 Issue 11

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

Annualized Return	Annualized Goal	Outperformance
12.0%	Mid-High Single Digits	4.5pts

60 basis points better than the SDY per annum

*Please see note below regarding performance measurement.

INSIDE THIS ISSUE

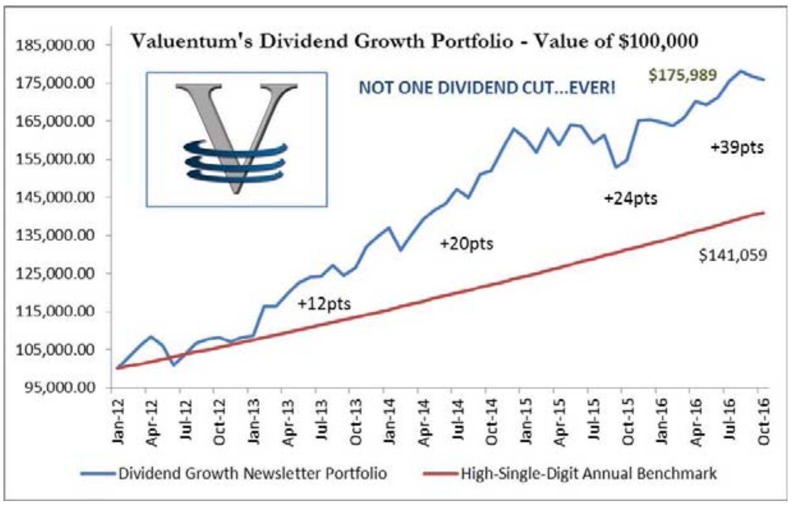
"Remember – not all dividends/distributions are created equal, and the sobering S&P 500 total payout data, is yet more evidence of the use of external capital by executive teams to pad cash returns to shareholders."
– Kris Rosemann

Are S&P 500 Stocks Returning Too Much Cash to Shareholders?

By Kris Rosemann

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, SDY, VNQ**

***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, November 1, 2016, the portfolio is significantly exceeding this goal.

How can any company return too much cash to its shareholders, right?

Well, let's first start this discussion of recent capital allocation trends with some clarifying thoughts. We're not against corporations returning excess capital to shareholders via dividends and buybacks (SPYB, PKW), provided they are value-generating moves. In many ways, we're just as excited as the rest of the market about generating sustainable and growing income via strong dividend paying equities, as evidenced by the existence of the Dividend Growth Newsletter and the strong performance of its namesake portfolio since inception. However, much of the recent rush to return shareholder cash back to owners may not be as it seems, as it is in part being fueled by external capital market support and comparatively lower yields on fixed-income securities.

As of the second quarter of 2016, for example, the dividend yield on S&P 500 (SPY) companies was 2.07%, more than 40 basis points higher than the US 10-year Treasury yield (IEF) of 1.65%, a benchmark for the risk-free rate and the foundation upon which risk spreads are added to price debt instruments. Under these conditions, could some investors and financial advisors be choosing to replace the bond portion of their managed investment portfolios

Please see *Are S&P 500...*on next page

*Are S&P 500…*from previous page

with riskier income or dividend growth stocks, in part or completely? The long-term implications have yet to be calculated precisely, but if this is the case, we posit that, in the event of a tipping point in the yield differential between dividend-paying stocks and yield instruments (where Treasury rates increase materially higher than the yields of most dividend-paying equities), asset flight away from some of the most overpriced dividend-paying entities may very well become a major theme under Federal Reserve contractionary monetary policy. The result? – lower stock prices.

With that said, let's comment on some of the recent trends in the board rooms regarding capital allocation decisions taking place across the broader market and specifically with S&P 500 companies. Total payouts to shareholders, which include dividends and buybacks, are approaching an all-time high in 2016 as the measure is on track to reach $1 trillion this year, according to Barclays. The mix for the year is expected to break down to an approximate 60/40 ratio in favor of share repurchases. What's more, dividends paid per share reached an all-time high in the trailing twelve month period ending with the second quarter of 2016. The idea of total payouts to shareholders growing isn't necessarily a bad thing in itself, but when considering surrounding circumstances, namely the potential asset allocation shift away from fixed-income into dividend-paying equities, the trend becomes a bit more concerning.

The dividend payout ratio (dividends per share divided by earnings per share) of S&P 500 companies in the twelve month period ending in the second quarter of 2016 reached 39.5%, a multiple percentage point increase on a year-over-year basis and the index's highest dividend payout ratio since the third quarter of 2009. Furthermore, the 6% growth in dividends-per-share for these companies in the twelve months ended June 30, 2016, does not correlate favorably with the index's earnings-per-share falling for the fifth consecutive quarter in the second quarter of 2016. In addition to the aggregate payout ratio being elevated compared to traditional measures, 42 individual companies have payout ratios exceeding 100% over the same measurement period. Of those 42 firms, 20 came from the real estate sector (REITs whose dividend health is dependent on access to capital markets), 4 from the energy sector, and 3 from both the materials and information technology sectors. Could management teams be stretching too far to please?

A collective dividend payout ratio of ~40% is not all that concerning for an established company, as many in the S&P 500 are, but some red flags come along with total shareholder distributions (buybacks and dividends) taking up 120%+ of aggregate earnings in the S&P 500 in the twelve month period ending with the second quarter of 2016. For one, this marks the second-highest level on a trailing twelve month basis since the Financial Crisis, though with little consolation we mention the first quarter of this year was the only higher mark. Interestingly, when total payouts (dividends + buybacks) of 100%+ reported earnings are breached, the ensuing years aren't all that great for equity prices. For example, in the previous three cases that this happened, it was followed by the Financial Crisis (2009-2010), the dot-com bust (2003-2004), and the recession of the early 1990s. Incredibly, total shareholder distributions have now exceeded aggregate earnings on a trailing twelve month basis *in each quarter since the second quarter of 2015* (source: S&P, Haver, Barclays).

So where are firms getting all of this cash to return to shareholders if it's not coming from earnings and/or internally-generated cash flows? Well, a growing number of companies are raising debt, in many cases, only to turn around and hand it right to shareholders. In fact, the S&P 500 has added roughly $1 trillion in debt during the past three years, and a large portion of that has been spent on dividends and buybacks. When one traditionally thinks of reasons for a business raising capital, uses such as growth projects, maintenance, and other tangible investments come to mind, not capital structure transformations or one-time distributions. Most peculiar, however, is that buybacks (a way to magnify leverage, especially if debt-funded) could arguably not come at a more inopportune time for shareholders. According to FactSet, the forward price-to-earnings ratio on S&P 500 companies stands at ~16.4 times, at the time of this writing, higher than both its 5-year and 10-year averages. We recognize the intricacies of tax- and interest-efficient corporate strategies that employ the use of

Please see *Are S&P 500…*on next page

***Are S&P 500…*from previous page**

issuing new debt, but buying back arguably significantly overpriced stock in large quantities is value-destructive to owners.

Please see our discussion of share buybacks, part of our Financial Analysis 501 series here >> http://www.valuentum.com/articles/20131028_1

In light of recent sluggish global economic growth trends, there is also strong case that the increase in total shareholder payouts by S&P 500 companies may be a function of diminished expected returns on future potential capital investments, in addition to appeasing the increased demand for dividend income by equity investors. What the extremely elevated level of total cash returns to owners relative to earnings might imply for the pace of future global economic growth may suggest tough times to come, if the best course of action is simply to give shareholders their money back. Some of the core holdings in the Dividend Growth Newsletter portfolio have been among the biggest returners of capital to shareholders. Among the top spenders on dividends in the twelve month period ending June 30, for example, were Apple (AAPL), Microsoft (MSFT), and Procter & Gamble (PG). Unlike entities that may be overpaying for their own stock, however, Apple is underpriced (buying back stock is a good thing in this case), Microsoft reasonably priced (a value-neutral dynamic), while Procter & Gamble continues works to finalize its brand transformation (buybacks continue to be assessed).

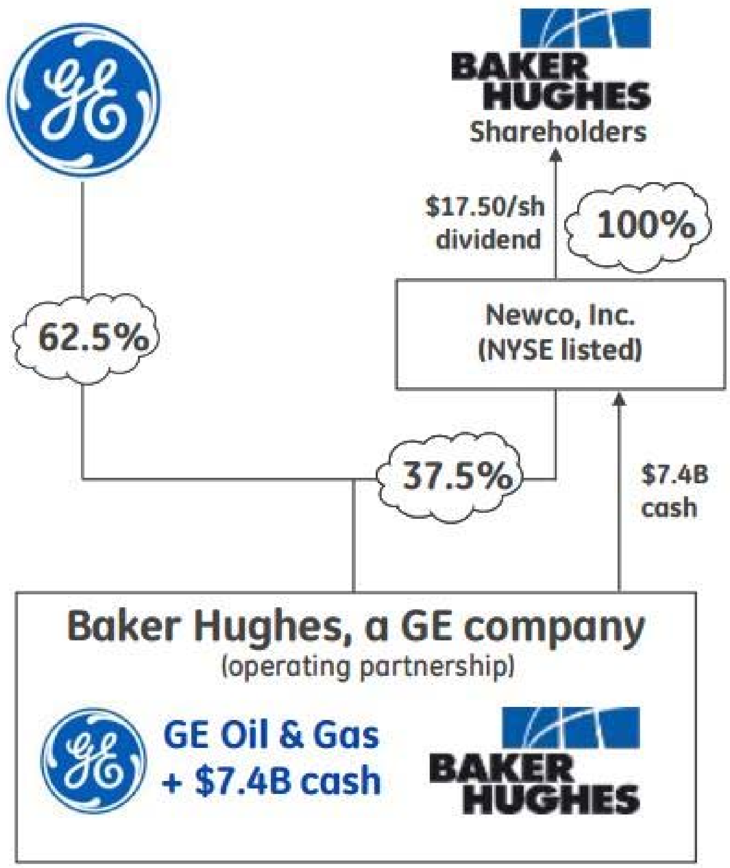
Why is this conversation important? Well, if or when the yield spread between dividend-paying equities and fixed income vehicles closes considerably (or inverts), a flight to higher-yielding fixed income instruments may take place, pressuring the equity prices of dividend-paying stocks (an asset flight dynamic). Second, under such conditions, borrowing costs will have risen, and access to capital will become increasingly more difficult, meaning that padding total shareholder payouts with external debt capital will become more challenging (lower dividend growth or more dividend cuts). It is for this very reason that we continue to prefer dividend payers whose payouts are funded by internal cash flows, as measured by cash flow from operations less all capital spending. In particular, we continue to witness distribution cuts across the MLP (AMLP) universe, the latest of which are Stonemor Partners (STON) and Martin Midstream (MMLP). Other MLPs such as Memorial Production (MEMP), EV Energy (EVEP) and Midcoast Energy (MEP) have faced considerable selling pressure.

Please don't get us wrong. We still very much like many dividend-paying entities, provided the entities are undervalued relative to our estimate of their intrinsic value (or in the ballpark under today's frothy market conditions) and that they can cover their future cash dividend payouts with internally-generated free cash flow (CFO less all capex), bolstered by a balance sheet that is overflowing with excess net cash (total cash less total debt on the balance sheet). Remember – not all dividends/distributions are created equal, and the sobering S&P 500 total payout data, revealed above, is yet more evidence of the use of external capital by executive teams to pad cash returns to shareholders. We continue to lean heavily on the forward-looking, cash-flow based Dividend Cushion ratio in our dividend analysis, and it continues to highlight dividend disappointments far in advance of impending cuts. Its most recent highlights, for example, included warning about the cuts in the payouts of Oceaneering (OII), Stonemor, and Noble Energy (NE).

Be sure to continue monitoring the Dividend Cushion ratios of the holdings in your own portfolio! If this may be our only feature you use, it alone could very well pay for itself, hundreds of times over. Just look at what happened to Stonemor, an entity with a very poor Dividend Cushion ratio, and its unitholders of late. Not only have unit prices of the MLP collapsed but investors that are still holding on are now stuck with reduced income—a double whammy. We hope you enjoy this November edition of the Dividend Growth Newsletter!

GE Positioning for Long-term Crude Oil Price Recovery

By Kris Rosemann



General Electric (GE) is betting big on energy these days, even as orders continue to decline in its 'Oil & Gas' segment as a result of continued pressure on energy resource pricing (USO, NGAS). The industrial conglomerate on October 31 agreed to merge the business with energy services giant Baker Hughes (BHI) to create a powerhouse in the sector with estimated $32 billion in annual revenue. Although we're very cautious on the deal based on the current operating environment and uncertainty in the energy markets--GE is expecting operating income in its Oil & Gas business to be down 30% in 2016--we think both companies are taking the right approach when considering the reasonable expectations embedded in the transaction. We continue to like GE's sprawling industrial portfolio.

GE has agreed to pay $7.4 billion in cash for a one-time special dividend of $17.50 for each share of Baker Hughes, and the merger proceedings are expected to result in GE owning 62.5% of the new, publicly-traded company with Baker Hughes' shareholders owning the remaining 37.5%. The deal is expected to close by mid-2017, and GE anticipates earnings accretion of $0.04 per share by 2018 (and $0.08 by 2020). It has projected ~$1.6 billion in run-rate synergies by 2020, ~$1.2 billion of which are expected to be of the cost savings variety. Such cuts are anticipated after GE completes more than $1 billion in cost reductions in its 'Oil & Gas' business in 2015 and 2016, and synergies are expected even with the continuation of a challenging outlook for crude oil prices, "Commodity Price Pressures Dinging Industrial Bellwether Expectations." Proforma EBITDA margins are anticipated at ~23% by 2020 on ~$34 billion in revenue.

With GE assuming crude oil prices in the $45-$60 range through 2019 in its evaluation of the merits of the deal, we think the tie-up is based on rational assumptions. Though downside risk related to energy resource pricing is still very much a reality, we would have been considerably more concerned about the benefits of such a transaction if it hinged on crude oil prices returning to triple-digit levels, not seen now

Please see *GE Positioning…*on page 6

The Dividend Growth Portfolio

Annualized Return	Annualized Goal	Outperformance
12.0%	Mid-High Single Digits	4.5pts

60 basis points better than the SDY per annum

DIVIDEND GROWTH PORTFOLIO -- as of November 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	65.48	6,613.48	3.8%	246.44
Apple (AAPL)	7/24/2013	63.17	51	3,228.45	111.49	5,685.99	3.3%	116.28
Cisco (CSCO)	11/14/2014	26.31	199	5,242.53	30.48	6,065.52	3.5%	206.96
Coach (COH)	9/19/2014	37.55	80	3,011.00	36.68	2,934.40	1.7%	108.00
Cracker Barrel (CBRL)	2/1/2016	133.50	18	2,410.00	134.83	2,426.94	1.4%	82.80
Energy Sector SPDR (XLE)	4/1/2015	72.63	121	8,795.76	68.63	8,304.23	4.8%	220.89
General Electric (GE)	10/21/2013	26.18	240	6,290.20	28.88	6,931.20	4.0%	220.80
Hasbro (HAS)	12/30/2011	31.89	110	3,514.90	82.21	9,043.10	5.2%	224.40
Intel (INTC)	12/30/2011	24.25	289	7,015.25	34.52	9,976.28	5.8%	300.56
Johnson & Johnson (JNJ)	12/30/2011	65.58	107	7,024.06	115.34	12,341.38	7.1%	342.40
Medtronic (MDT)	12/30/2011	38.25	157	6,012.25	80.92	12,704.44	7.3%	270.04
Microsoft (MSFT)	12/30/2011	25.96	77	2,005.92	59.80	4,604.60	2.7%	120.12
Proctor & Gamble (PG)	12/30/2011	66.71	105	7,011.55	86.85	9,119.25	5.3%	281.40
PP&L (PPL)	12/30/2011	29.42	238	7,008.96	34.00	8,092.00	4.7%	361.76
Realty Income (O)	7/24/2013	44.35	60	2,668.00	57.74	3,464.40	2.0%	145.20
S&P Dividend ETF SPDR (SDY)	4/20/2016	81.33	105	8,546.65	80.67	8,470.35	4.9%	210.91
Vanguard REIT ETF (VNQ)	2/1/2016	77.07	32	2,473.24	79.98	2,559.36	1.5%	93.16
Cash -- changes in monthly cash balance reflects dividends received and tradin				2,363.42		54,014.73	31.2%	3,552.12
Dividend Growth Portfolio				100,000.00		**173,351.65**	100.0%	**TBD**
DG Portfolio Annualized Return (from inception through current date)								**12.0%**
DG Portfolio Annualized Return Goal (Mid-to-High Single Digit Returns)								7.5%
DG Portfolio Annualized Return Outperformance								**4.5%**
SPDR S&P Dividend ETF (SDY)								**11.4%**

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

DIVIDEND GROWTH PORTFOLIO -- as of November 1, 2016								Fundamental data as of November 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)	2.44	3.73%	mid-Dec 2016	mid Dec 2016 (quart)	1.2	GOOD	GOOD	$58.00	6	1.13
Apple (AAPL)	2.28	2.05%	early Nov 2016	Nov 2016 (quart)	4.7	EXCELLENT	EXCELLENT	$147.00	7	0.76
Cisco (CSCO)	1.04	3.41%	early Jan 2017	early Jan 2017 (quart)	2.8	EXCELLENT	EXCELLENT	$39.00	7	0.78
Coach (COH)	1.35	3.68%	early Dec 2016	early Dec 2016 (quart)	1.9	GOOD	GOOD	$41.00	3	0.89
Cracker Barrel (CBRL)	4.60	3.41%	mid Jan 2017	late Jan 2017 (quart)	1.7	GOOD	GOOD	$171.00	6	0.79
Energy Sector SPDR (XLE)	1.83	2.66%	late Dec 2016	early Dec 2016 (quart)	-	GOOD	NEUTRAL	-	UR	-
General Electric (GE)	0.92	3.19%	mid Dec 2016	Dec 2016 (quart)	3.1	EXCELLENT	GOOD	$32.00	6	0.90
Hasbro (HAS)	2.04	2.48%	late Jan 2017	late Jan 2017 (quart)	1.7	GOOD	EXCELLENT	$73.00	3	1.13
Intel (INTC)	1.04	3.01%	early Nov 2016	early Dec 2016 (quart)	2.6	GOOD	GOOD	$42.00	6	0.82
Johnson & Johnson (JNJ)	3.20	2.77%	late Nov 2016	early Dec 2016 (quart)	2.7	GOOD	EXCELLENT	$121.00	7	0.95
Medtronic (MDT)	1.72	2.13%	late Dec 2016	Dec 2016 (quart)	1.4	GOOD	EXCELLENT	$76.00	6	1.06
Microsoft (MSFT)	1.56	2.61%	mid Nov 2016	mid Dec 2016 (quart)	2.7	GOOD	EXCELLENT	$52.00	3	1.15
Proctor & Gamble (PG)	2.68	3.09%	late Jan 2017	early Feb 2017 (quart)	1.5	GOOD	EXCELLENT	$70.00	6	1.24
PP&L (PPL)	1.52	4.47%	early Dec 2016	early Dec 2016 (quart)	Held for diversification reasons.			$33.00	3	1.03
Realty Income (O)	2.42	4.19%	monthly	monthly	2.1	GOOD	GOOD	$59.00	3	0.98
S&P Dividend ETF SPDR (SDY)	2.01	2.49%	mid Dec 2016	late Dec 2016	-	-	-	-	UR	-
Vanguard REIT ETF (VNQ)	2.91	3.64%	late Dec 2016	Dec 2016 (quart)	-	GOOD	NEUTRAL	-	UR	-

*GE Positioning…*from page 4

for some time. There's no guarantee crude oil prices will ever reach those levels again either. In any case, the prospective company figures to take full advantage of a potential recovery in the price of crude oil over time, as it will be the second-largest oil field service company in terms of revenue behind only Schlumberger (SLB). GE is not expecting a recovery to take place overnight in Baker Hughes' operations though; it anticipates the firm returning to only ~60% of its peak EBITDA (achieved in 2014) by 2020.

Generally speaking, we like the deal for both sets of shareholders, but let's talk Baker Hughes first. Baker Hughes' shareholders will receive a special dividend of approximately 30% of Baker Hughes' share price prior to the deal announcement in addition to 37.5% equity ownership in a new, stronger company with material opportunities for synergies. The financial backing of GE is also quite the asset should tough times in the energy-services space ensue. Though rig and well counts have improved slightly in recent months, activity across the energy sector remains well below that of years past, as US rig and well counts in the third quarter of 2016 were about half that of the comparable period in 2015. Still, the combined entity is expected to provide top-notch productivity solutions as digital capabilities become an increasingly important part of energy resource exploration, production, transportation, and refining. The risk for both sets of shareholders largely rests in the event the combined entity falls short in extracting estimated synergies (as both are beholden to the energy resource pricing environment under any condition). We like that the 'new' Baker Hughes will not have to take on any additional debt to complete the transaction.

General Electric, on the other hand, will use debt to finance the $7.4 billion cash special dividend to Baker Hughes shareholders. While we are not particularly fond of the application of leverage in the transaction, a cash-rich conglomerate such as GE can do so without materially affecting its credit quality. Presentation materials suggest that there will be no anticipated credit rating impact from the transaction, and the divestitures of a number of its financial assets have given the industrial giant additional financial flexibility (GE is no longer a SIFI, or a systemically important financial institution). Because GE will be borrowing from GE Capital, its captive financing arm, the debt associated with this transaction is anticipated to be at no incremental cost to the firm through 2019. Additionally, GE expects free cash flow conversion of the new company to be ~90% by 2020 and an incremental ~$1 billion in free cash flow by 2019, revealing considerable potential for meaningful long-term value creation.

Along with a transaction of this nature come restructuring and integration efforts, which place an additional amount of attention on GE's ongoing capital allocation plans. The industrial giant plans to sell GE Water, and it is currently in talks with prospective buyers, targeting a mid-2017 closing. The gain from the sale will fund restructuring and integration costs for the Baker Hughes deal, which could be up to $1 billion. Outside of the asset sale, GE remains committed to its capital allocation strategy. It continues to target the sustenance of an attractive dividend with a yield greater than that of peers, and it will continue to allocate dividends from GE Capital to its buyback program through 2018. Management remains very shareholder friendly.

That said, we're not jumping to conclusions just yet. It is prudent to note that the completion of the deal is not yet set in stone, as regulatory approval is not yet finalized. Close followers of Baker Hughes' stock recently saw its deal with Halliburton (HAL) nixed by the US Department of Justice as a result of its perception of the deal's impact on competition across the energy services industry (OIH, XES, IEZ, PXJ). However, a much more limited amount of product overlap is present in the proposed GE-Baker Hughes tie-up, suggesting that the deal has a greater likelihood of consummation (in the event the deal is not completed, GE would have to pay Baker Hughes $1.3 billion). Halliburton ended up paying Baker Hughes a $3.5 billion termination fee.

From a long-term value-creation point of view, we generally like the deal for GE shareholders. Combining assets in similar end markets, extracting cost savings from such assets, reducing some

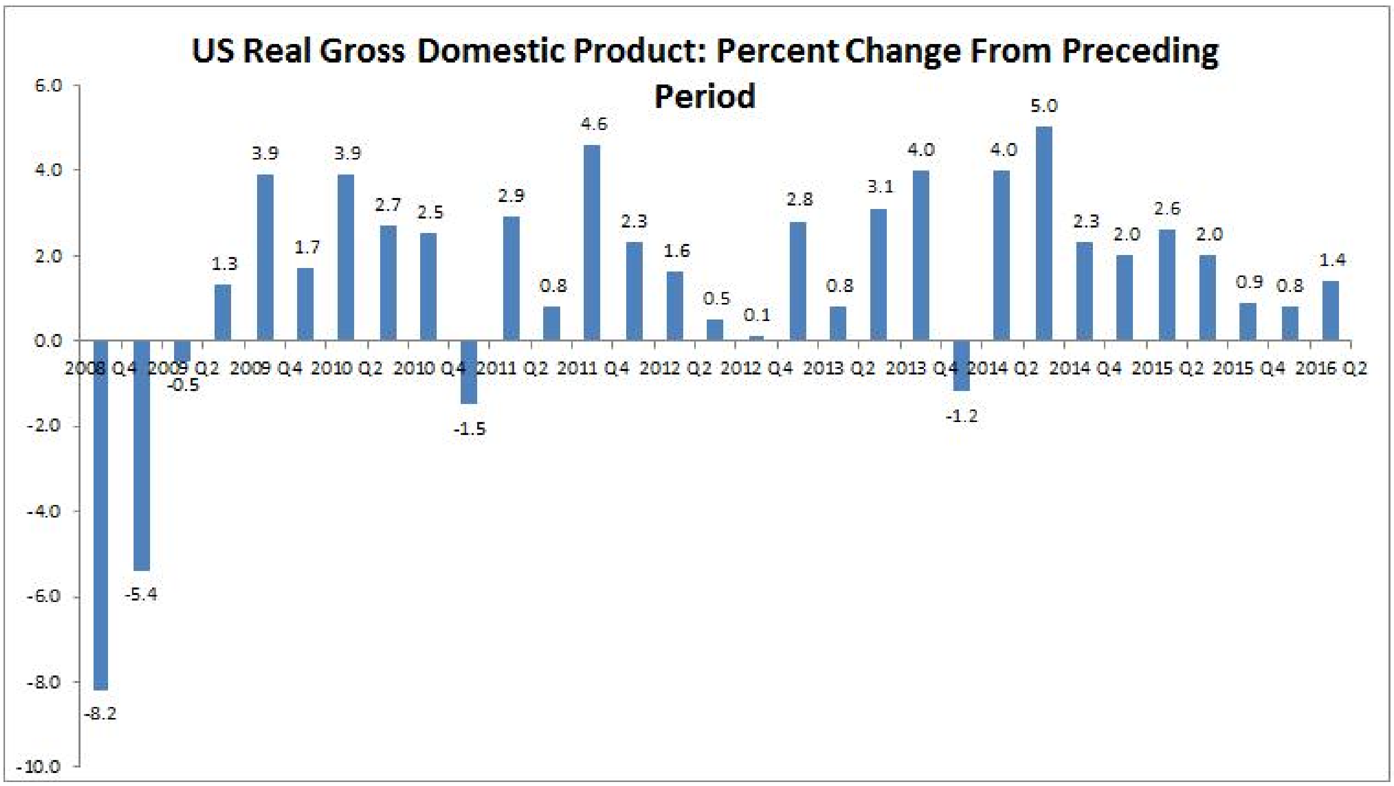
Please see *GE Positioning…*on next page

*GE Positioning…*from previous page

competition, and setting the stage for improved energy-service pricing makes a lot of sense, even if the future path of crude oil pricing may play the most important role in how much we like transaction over the long haul (something out of both companies' control). GE retains its well-diversified industrial portfolio, including its very valuable aerospace business, and will now have a material equity interest in an energy services powerhouse to nurture as it puts its SIFI-designation behind it. Though GE's reported results will continue to be "messy" in light of all the corporate transactions of late, we continue to like shares of the company in the newsletter portfolios. Its free-cash-flow-supported dividend yield north of 3% is very hard to pass up. Our fair value estimate of GE is $32 per share.

Commodity Price Pressures Dinging Industrial Bellwether Expectations

By Kris Rosemann



Commodity resource prices, while suppressed, are said to be stabilizing, but stabilization at low levels does little good for many operators tied to commodity-based end markets. Such is the case for several industrial giants General Electric (GE), 3M (MMM), and Caterpillar (CAT), all of which have seen their worldwide operations impacted by the effect that a prolonged trough in commodity prices has had on global economic growth, "Industrial Bellwethers Hit by Global Economic Growth Concerns." We recently highlighted the organic growth pressures industrial bellwether Honeywell (HON) has been experiencing, "Honeywell's Stock Up 170% Since End of 2009; GE a Better Bet?" and its peers have been echoing its concerns.

GE reported third-quarter earnings October 21, and while the report itself was decent, the company trimmed its 2016 revenue outlook. We're still huge fans of GE's business transformation, and the company remains a core holding of both newsletter portfolios, "GE Continues Transformation; Steady Growth at Honeywell (April 2016)." No longer is GE held back by its financials business, and its industrial assets and cash-flow generating capacity are some of its greatest attributes. It still wasn't great to see a

Please see *Commodity Price…*on next page

*Commodity Price…*from previous page

shift in the trajectory of internal expansion at the industrial behemoth. Organic revenue for the firm as a whole in 2016 is now expected to be in a range of flat-to-up-2% compared to previous guidance of growth in the 2%-4% range, not a huge change, but directionally significant in light of peer performance.

The culprit? You guessed it – low commodity prices as "challenges continue in the resource sector." GE continues to pump its acquisition of Alstom's power business, which is on track to meet expectations in 2017 and 2018, and the industrial giant continues to report a burgeoning backlog (~$320 billion) thanks in part to performance of its 'Aviation' and 'Healthcare' segments, but it expects a more challenging environment to persist for its 'Oil & Gas' segment and related end markets. With energy resource prices, namely crude oil, still lingering around a third of the levels seen prior to the Financial Crisis, the operating environment isn't as easy as it once was (organic revenue in its 'Oil & Gas' division dropped 20% in the third quarter). That's a pretty steep decline that will ease a bit in the fourth quarter, per management's guidance calling for a 10% slip, but it's also worth mentioning that organic revenue growth across the remainder of GE's businesses continues to be solid, up 4% through the first three quarters of the year (if we exclude the much-beleaguered 'Oil & Gas' division).

Despite the reduction in organic top-line growth expectations, GE maintained the $1.50 midpoint of its earnings per share guidance for full-year 2016, though it narrowed the guidance range to $1.48-$1.52 from $1.45-$1.55. The resilient bottom-line in the face of a slowing pace of sales expansion continues to be helped by GE's ability to extract cost savings in the 'Oil & Gas' segment, with the company now expecting to deliver between $700-$800 million in savings in 2016 compared to initial expectations of $400 million. However, the aggressive cost cutting in 2016 may leave little room for further cost optimization in 2017, in which management is not expecting a material recovery in energy resource pricing.

Industrial conglomerate peer 3M is experiencing very similar dynamics in its global industrial operations. 3M reported third-quarter results October 25. Each of the innovative firm's operating segments generated revenue growth on an as-reported basis, except for its 'Electronics and Energy' segment, where energy-related sales fell 9% on a year-over-year basis. The company reduced its expectations for full-year 2016 organic revenue growth for the second time in as many quarters, as it now expects organic revenue to be approximately flat compared to previous guidance of growth in a range of 0%-2% and initial guidance of 1%-3%. Nevertheless, 3M was able to deliver its 100th consecutive year of paying a dividend and has now increased its payout in each of the last 58 years as of the third quarter of 2016.

Equipment manufacturer Caterpillar has probably been the poster-child of companies punished by the ongoing slump in commodity prices during the past 18-24 months. In 2016, the firm expects to report its fourth consecutive year of sales declines for the first time in its history, and it reduced its guidance for the year after another weak quarterly report October 25. In its third-quarter report, released October 26, the equipment maker said that it now expects 2016 revenue to come in at ~$39 billion compared to previous guidance of $40-$40.5 billion, and profit per share excluding restructuring costs guidance has been reduced to $3.25 from $3.55. Caterpillar is not expecting the challenges it is facing to disappear in 2017, and we can't say we are either. Management does not expect a significant difference in 2017 performance compared to 2016 performance, and CEO Doug Oberhelman plans to retire in March 2017.

All things considered, not a lot has changed with respect to our outlook on the global industrial operating environment and how we're playing it. The diversification of GE's sprawling digital industrial portfolio provides ample downside protection in our minds (not to mention its dividend yield), and we love the upside potential that exists in its investments in clean energy and 3D printing, though the latter has come into question of late. The most recent quarterly report was a direct example of this diversification, as management reiterated its $2 per share earnings target for 2018, despite materially weaker performance from its 'Oil & Gas' segment than was anticipated in April 2015 when the target was initially set.

Please see *Commodity Price…*on next page

*Commodity Price...*from previous page

GE continues to be at the forefront of this generation's version of an industrial revolution as the adaptation of digital capabilities in manufacturing spreads. With its financial segment no longer a material headwind during tough times of credit, GE's dividend remains on solid ground, in our view, with a yield of ~3.2% and a raw, unadjusted Dividend Cushion ratio of 1.6. Our fair value estimate of GE is $32 per share, and we plan to keep the positions in both the Best Ideas Newsletter portfolio and the Dividend Growth Newsletter portfolio intact. The company's performance, however, will continue to ebb and flow with the industrial and commodity cycle.

Earnings Insight -- Apple

By Brian Nelson, CFA

What management said:

"Our strong September quarter results cap a very successful fiscal 2016 for Apple," said Tim Cook, Apple's CEO. "We're thrilled with the customer response to iPhone 7, iPhone 7 Plus and Apple Watch Series 2, as well as the incredible momentum of our Services business, where revenue grew 24 percent to set another all-time record...We are pleased to have generated $16.1 billion in operating cash flow, a new record for the September quarter," said Luca Maestri, Apple's CFO. "We also returned $9.3 billion to investors through dividends and share repurchases during the quarter and have now completed over $186 billion of our capital return program."

The scoop:

Revenue and earnings per share were largely in-line with expectations in the period, but all key products segments experienced declining units sold, with the largest decline witnessed in Macs (down 14%); services revenue was the bright spot at 24% year-over-year expansion. We're not reading much into management's projections for its fiscal first quarter of 2017, where revenue is targeted at $76-$78 billion, gross margin at 38%-38.5%, and operating expenses at $6.9-$7 billion. Revenue guidance may have come in a little light relative to consensus expectations, and expansion in China (FXI) appears more challenging than originally thought, but the company's gross margin rate is still quite healthy. The latest iteration of the iPhone, the iPhone 7 and iPhone 7 Plus, remain in high demand, and rumors about an "Apple car" and "Apply TV" continue to swirl. The company's AirPods are highly-anticipated, though opinions vary.

Insight from the quarterly conference call:

"As you know, iPhone customers are the most satisfied and loyal customers in the world, and fiscal 2016 saw more customers switch from Android (GOOG, GOOGL) to iPhone than ever before. This is due to the superior customer experience we deliver with our products, and it's something no other company can match." – CEO Tim Cook

"iPhone sales in Greater China declined during the quarter, but the initial customer response to iPhone 7 and 7 Plus gives us confidence that our December quarter performance in China will be significantly better on a year-over-year basis than our September quarter results, even as we lap the all-time record period from a year ago." – CFO Luca Maestri

Are we changing our minds with our position?:

No. Apple remains a core holding in both newsletter portfolios, and the company's mindshare of the consumer is arguably as valuable as its ecosystem. Apple remains an innovator, and whether through internal R&D or through a future acquisition, we expect the company to remain at the forefront of the technology revolution in mobile and beyond. A huge net cash balance and a nice and growing dividend offer substantial support for a position in both newsletter portfolios.

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
Omega Healthcare	OHI	Financials	6.8%	9	EXCELLENT	1.5
Western Gas	WES	Energy	6.3%	6	EXCELLENT	1.7
Brookfield Infrastructure	BIP	Energy	4.9%	6	EXCELLENT	1.2
Cypress Semi	CY	Information Technology	4.2%	6	GOOD	1.5
Entergy	ETR	Energy	4.2%	6	GOOD	1.4
Diebold	DBD	Industrials	4.1%	6	GOOD	1.3
Philip Morris	PM	Consumer Staples	4.1%	6	GOOD	0.6
QUALCOMM	QCOM	Information Technology	4.0%	7	EXCELLENT	3.0
Caterpillar	CAT	Industrials	3.9%	7	GOOD	0.6
Abercrombie & Fitch	ANF	Consumer Discretionary	3.9%	6	GOOD	2.7
Weyerhaeuser	WY	Materials	3.8%	6	GOOD	1.5
Cummins	CMI	Industrials	3.6%	6	EXCELLENT	1.8
Gap	GPS	Consumer Discretionary	3.6%	7	EXCELLENT	2.1
Darden Restaurants	DRI	Consumer Discretionary	3.6%	7	GOOD	1.3
IBM	IBM	Information Technology	3.5%	6	EXCELLENT	1.5
Taiwan Semiconductor	TSM	Information Technology	3.5%	6	EXCELLENT	2.3
Hewlett-Packard	HPQ	Information Technology	3.5%	6	GOOD	2.1
Altria Group	MO	Consumer Staples	3.5%	6	GOOD	1.2
ABB	ABB	Industrials	3.5%	6	GOOD	1.6
Reynolds American	RAI	Consumer Staples	3.4%	6	GOOD	0.6
Cisco	CSCO	Information Technology	3.4%	7	EXCELLENT	2.8
Cracker Barrel	CBRL	Consumer Discretionary	3.4%	6	GOOD	1.7
Procter & Gamble	PG	Consumer Staples	3.2%	6	EXCELLENT	1.5
Western Union	WU	Information Technology	3.2%	6	EXCELLENT	2.4
Intel	INTC	Information Technology	3.1%	6	GOOD	2.6
Bristol-Myers Squibb	BMY	Health Care	3.1%	6	GOOD	2.0
CA Tech	CA	Information Technology	3.1%	7	GOOD	3.0
AVX Corp	AVX	Information Technology	3.0%	6	EXCELLENT	3.6
Xerox	XRX	Industrials	3.0%	9	EXCELLENT	1.6
Merck	MRK	Health Care	2.9%	6	GOOD	1.9
General Electric	GE	Industrials	2.9%	6	GOOD	3.1

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 October 31, 2016 Fundamental data as of October 31, 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)	4.44	2.69%	1.4	GOOD	EXCELLENT	$133.00	4	1.24	165.30
Abbott (ABT)	1.04	2.65%	2.7	GOOD	EXCELLENT	$43.00	3	0.91	39.24
AbbVie (ABBV)	2.56	4.59%	1.4	GOOD	EXCELLENT	$74.00	4	0.75	55.78
ADP (ADP)	2.12	2.44%	6.2	EXCELLENT	EXCELLENT	$98.00	6	0.89	87.06
Analog Devices (ADI)	1.68	2.62%	2.3	GOOD	EXCELLENT	$53.00	6	1.21	64.10
Becton, Dickinson (BDX)	2.64	1.57%	0.7	POOR	VERY POOR	$161.00	7	1.04	167.91
Boeing (BA)	4.36	3.06%	2.0	GOOD	EXCELLENT	$124.00	3	1.15	142.43
Coca-Cola (KO)	1.40	3.30%	1.4	GOOD	EXCELLENT	$39.00	4	1.09	42.40
Colgate-Palmolive (CL)	1.56	2.19%	1.7	GOOD	EXCELLENT	$60.00	6	1.19	71.36
Deere (DE)	2.40	2.72%	1.1	POOR	VERY POOR	$93.00	3	0.95	88.30
Dover (DOV)	1.76	2.63%	1.1	POOR	VERY POOR	$64.00	4	1.05	66.89
DuPont (DD)	1.52	2.21%	2.4	GOOD	GOOD	$62.00	6	1.11	68.79
Eli Lilly (LLY)	2.04	2.76%	1.9	GOOD	GOOD	$73.00	6	1.01	73.84
General Dynamics (GD)	3.04	2.02%	3.0	EXCELLENT	EXCELLENT	$129.00	6	1.17	150.74
Genuine Parts (GPC)	2.63	2.90%	1.9	GOOD	EXCELLENT	$88.00	6	1.03	90.59
H&R Block (HRB)	0.88	3.83%	1.6	GOOD	GOOD	$28.00	3	0.82	22.97
Harris (HRS)	2.12	2.38%	0.1	VERY POOR	VERY POOR	$92.00	7	0.97	89.21
Honeywell (HON)	2.66	2.43%	2.9	EXCELLENT	EXCELLENT	$106.00	6	1.03	109.68
Hormel Foods (HRL)	0.58	1.51%	2.7	GOOD	EXCELLENT	$42.00	6	0.92	38.50
IBM (IBM)	5.60	3.64%	1.5	GOOD	EXCELLENT	$164.00	6	0.94	153.69
Illinois Tool Works (ITW)	2.60	2.29%	1.8	GOOD	EXCELLENT	$88.00	1	1.29	113.57
Kimberly-Clark (KMB)	3.68	3.22%	1.2	GOOD	GOOD	$112.00	7	1.02	114.41
Lockheed Martin (LMT)	6.60	2.68%	1.2	POOR	VERY POOR	$193.00	1	1.28	246.38
Merck (MRK)	1.84	3.13%	1.9	GOOD	GOOD	$55.00	6	1.07	58.72
Northrop Grumman (NOC)	3.60	1.57%	1.8	GOOD	EXCELLENT	$160.00	1	1.43	229.00
Paychex (PAYX)	1.84	3.33%	2.6	GOOD	EXCELLENT	$48.00	4	1.15	55.20
Phillip Morris (PM)	4.16	4.31%	0.6	GOOD	GOOD	$84.00	6	1.15	96.44
Raytheon (RTN)	2.93	2.14%	2.2	GOOD	EXCELLENT	$104.00	7	1.31	136.61
St. Jude (STJ)	1.24	1.59%	2.1	GOOD	EXCELLENT	$85.00	5	0.92	77.84
Texas Instr (TXN)	1.52	2.15%	2.1	GOOD	EXCELLENT	$54.00	6	1.31	70.85
United Technologies (UTX)	2.64	2.58%	1.4	GOOD	EXCELLENT	$107.00	7	0.96	102.20
UPS (UPS)	3.12	2.90%	1.7	GOOD	EXCELLENT	$100.00	6	1.08	107.76
VF Corp (VFC)	1.68	3.10%	2.0	GOOD	EXCELLENT	$55.00	5	0.99	54.21
Walgreens (WBA)	1.50	1.81%	2.3	GOOD	EXCELLENT	$75.00	6	1.10	82.73

UR = Under Review

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
CONSOL Energy	CNX	Industrial Minerals	0.3%	VERY POOR	-70.4
KB Home	KBH	Homebuilders	0.7%	VERY POOR	-38.9
Windstream	WIN	Telecom Services - diversified	6.7%	VERY POOR	-36.1
Lennar	LEN	Homebuilders	0.3%	VERY POOR	-25.6
Devon Energy	DVN	Independent Oil & Gas	0.6%	VERY POOR	-21.3
Anadarko	APC	Independent Oil & Gas	0.3%	VERY POOR	-12.7
Ryder System	R	Rental and Leasing	2.5%	VERY POOR	-8.5
Tailored Brands	TLRD	Retail - Men's, Women's, Kids' Apparel	5.0%	VERY POOR	-7.1
Yamana Gold	AUY	Metals & Mining - gold	0.4%	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
D. R. Horton	DHI	Homebuilders	1.0%	VERY POOR	-5.3
ConocoPhillips	COP	Major Oil & Gas	2.4%	VERY POOR	-4.9
Koppers	KOP	Building Materials	3.1%	VERY POOR	-4.5
MDC	MDC	Homebuilders	4.0%	VERY POOR	-4.4
Teekay	TGP	Shipping	4.9%	VERY POOR	-4.4
Barrick Gold	ABX	Metals & Mining - gold	0.4%	VERY POOR	-4.3
Hill-Rom	HRC	Medical Instruments	1.3%	VERY POOR	-4.2
Hess	HES	Refiners	1.8%	VERY POOR	-3.8
Murphy Oil	MUR	Refiners	4.4%	VERY POOR	-3.7
Ball Corp	BLL	Containers & Packaging	0.7%	VERY POOR	-3.7
Textainer	TGH	Rental and Leasing	8.7%	VERY POOR	-3.6
Rent-A-Center	RCII	Rental and Leasing	3.5%	VERY POOR	-3.3
Olin Corp	OLN	Chemicals - mid/small	3.9%	VERY POOR	-2.7
Noble Energy	NBL	Independent Oil & Gas	1.2%	VERY POOR	-2.7
Apache	APA	Independent Oil & Gas	1.7%	VERY POOR	-2.5
Natural Resource Partners	NRP	Industrial Minerals	11.4%	VERY POOR	-2.4
Wendy's Co	WEN	Restaurants - Fast Food & Coffee	2.2%	VERY POOR	-2.4
Deltic Timber	DEL	Building Materials	0.6%	VERY POOR	-2.3
Quad/Graphics Inc	QUAD	Book Publishing	4.8%	VERY POOR	-2.1
CF Industries	CF	Chemicals - agriculture	4.7%	VERY POOR	-2.0
Huntsman	HUN	Chemicals - broad	2.8%	VERY POOR	-2.0
Service Corp Intl	SCI	Personal Services	2.0%	VERY POOR	-1.9
Centurylink	CTL	Telecom Services - diversified	7.8%	VERY POOR	-1.7
Alcoa	AA	Aluminum	1.3%	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

AT&T Targeting Disruption in Transformational Merger

By Kris Rosemann

Key Takeaways

AT&T has agreed to acquire Time Warner for $85.4 billion in cash and stock in a deal that is expected to close by the end of 2017. Strict regulatory scrutiny can be expected.

The deal has the potential to disrupt the traditional pay-TV industry while setting AT&T apart from its competitors in the wireless telecom industry, where growth has become sparse for the firm.

The telecom industry is maturing, and price-slashing competition has changed the game as network differentiation has largely become a thing of the past.

We're not fans of the debt that will come with the completion of the deal, but the prospects of what the combined entities could produce are certainly interesting.

We view the additional debt as a distinct negative to AT&T's dividend health and the company's Dividend Cushion ratio. We continue to be cautious on AT&T's long-term dividend health.

AT&T (T) has agreed to acquire Time Warner (TWX) for $85.4 billion, evenly split between cash and stock, or $107.50 per share. When considering the impact of Time Warner's net debt, the total transaction value comes in at a whopping $108.7 billion. The deal is expected to close by the end of 2017, and is anticipated to result in the extraction of $1 billion in annual run rate cost synergies within 3 years of the deal closing.

On the surface, we like the deal for Time Warner shareholders, as our most recent fair value estimate for shares was $81, to which the deal price represents a substantial premium. The market appears to be currently pricing in a significant amount of regulatory pressure, however, as shares of both companies have reacted unfavorably to the announcement of the deal. We expect a modest haircut to our estimate of AT&T in light of its hefty price above our estimate of Time Warner's standalone intrinsic value.

In acquiring Time Warner, AT&T is addressing its needs to diversify as its traditional wireless business has hit a point of maturation and slowing growth. Intense price-cutting competition from the likes of Sprint (S) and T-Mobile (TMUS) helped cause the company to lose 268,000 mainstream wireless phone customers in the third quarter of 2016, and it also lost a net 3,000 video customers. Since the acquisition of DirecTV in 2015, the company has lost nearly 200,000 video customers as new additions in the DirecTV business have not been enough to outpace losses in its more dated U-Verse service.

Part of what has held AT&T's progress with its DirecTV acquisition back is its ongoing negotiations with content owners in its plans to launch an over-the-top video service that would allow users to stream programming on the Internet without a satellite dish called DIRECTV NOW. Such a service, expected to be launched by year-end, was one of the key drawings of the DirecTV deal, but negotiations with content owners have proved to be very difficult, which is where Time Warner comes in.

With the purchase of Time Warner, AT&T is gaining ownership of a premium content generator with impressive brands including HBO, CNN, TNT, and the Warner Bros. film and TV studio. The company is now "all-in" on its bet that mobile TV and video consumption will be the next growth driver for wireless telecom providers and is tying its future to the ownership of popular franchises such as Game of Thrones. The new AT&T aims to disrupt the traditional pay-television package market and push the boundaries in mobile content consumption in the US by creating an online-video bundle. While a deal in the $85 billion dollar range is certain to face regulatory scrutiny, AT&T officials believe that since the firm is not necessarily eliminating a competitor, concerns should be more easily addressable.

Those who remember Time Warner's tie up with AOL in 2000 may be hesitant to praise the deal, as the firms' endeavors eventually proved fruitless. However, proponents of the deal with AT&T, including Time Warner CEO Jeff Bewkes, have made a convincing case that Internet distribution has come a long way in

Please see *AT&T Targeting…*on next page

*AT&T Targeting…*from previous page

the past decade and a half, and the platforms from which consumers access content have evolved significantly. "Video is the future of mobile and the future of mobile is video."

In addition to the ownership of content significantly increasing the value potential of its own product offerings, AT&T expects to retain Time Warner's traditional content distribution network. Just as AT&T had found it difficult negotiating with content owners over the licensing of content for its proposed mobile-TV network, now others will come to it to negotiate licenses for channels like TNT, Cartoon Network, and HBO, further diversifying its revenue stream. Though AT&T is already materially tied to the ongoing consumer trend of cord-cutting in personal entertainment, the acquisition of Time Warner also comes with its 10% stake in streaming service Hulu.

If the deal is completed, the resulting AT&T would generate more than 40% of its revenue from its entertainment business, helping reduce its reliance on success in its wireless business. However, the deal is also expected to bring on an additional $60+ billion in debt. We don't like the idea of adding $23+ billion in Time Warner's debt and $40 billion in loans for the cash consideration of the deal to a balance sheet with a net debt position of nearly $120 billion as of the end of the third quarter of 2016, but management expects its net debt-to-adjusted EBITDA ratio to be near 2.5x by the end of the first year after the deal closes and has suggested it could approach 1.8x by the end of year four after closing.

These are reasonable leverage ratios for such an elevated debt load, but they leave little margin for error in operational execution and integration. Moody's (MCO) has since put AT&T's debt ratings on review for a possible downgrade as a result of the increased leverage. According to the rating agency, the financing costs associated with the deal will consume the majority of the free cash flow stream acquired due to increased cash dividend obligations and material additional after-tax interest expense.

In addition to the growth that is expected to come with AT&T's significantly enhanced video offerings, including the aforementioned bundling of mobile network and premium video content consumption, the Time Warner acquisition provides its business with diversification benefits. Time Warner will represent ~15% of total AT&T revenue, and Time Warner's exposure to Latin America via HBO Latin America provides the company with additional exposure to the television markets in 24 countries. Time Warner's business is also significantly less capital intensive and subject to fewer regulatory restrictions than AT&T's, which should help improve the firm's free cash flow margins and ultimately help it hit its deleveraging targets as well as improve dividend coverage.

The benefits of a combination of the transforming wireless network giant and a premium content generator are apparent when considering the fundamental shift in how consumers prefer to view video content, but AT&T's decision to go after the mobile video space so aggressively also highlights an issue in the broader wireless telecom space itself. Intense competition has resulted in slowing growth for bellwethers in the industry, and as we noted previously, AT&T has struggled in recent quarters and rival Verizon (VZ) has experienced a similar fate. The telecom giant reported third quarter revenue fell nearly 7% as net postpaid subscriber growth disappointed and postpaid subscriber churn rose above 1% for the first time in six quarters.

Price-slashing competition from T-Mobile has been a key factor in AT&T's and Verizon's subscriber addition woes in recent quarters, and the firm reported 2 million total net additions including 851k postpaid phone net subscriber additions in the third quarter of 2016—Verizon added just 446k— which marks the 14th consecutive quarter in which it has added more than 1 million total customers and the 11th consecutive quarter in which it was the industry leader in postpaid phone subscriber additions. The lack of differentiation between the networks of industry leaders like Verizon and growing competitors like T-Mobile has been a core driver in the shift of growth in the industry. As of the third quarter of 2016, T-Mobile claims to have a 4G LTE network offers 99.7% of the coverage of Verizon's competing network.

Please see *AT&T Targeting…*on next page

*AT&T Targeting…*from previous page

Such a dynamic is what has forced AT&T to become an aggressive player in the 'bundling' industry, which is likely to become a growing trend as companies continue to work to solve the new age consumer. Streaming services Netflix (NFLX) and Amazon (AMZN) are becoming increasingly vertically-integrated in creating their own content, and AT&T is searching for a similar dynamic with a mobile distribution focus. Apple (AAPL) has also been reported to be looking for its own original content creation, and while the future of Apple TV remains up for speculation, an integrated traditional-TV and mobile-based service from the company that has found its way into the everyday lives of consumers perhaps better than any other is somewhat easy to envision.

The AT&T-Time Warner deal also puts an increasing amount of pressure on Verizon to find its next step in differentiation. AT&T has beaten it to the punch in the mobile video content arena, and though Verizon remains the leader in the wireless telecom market, it cannot sit by idly as others slash prices and transform their business models. Cost cutting will inevitably be a focus as the industry continues to mature, and many expect Verizon to pull harder on the pricing lever to maintain market share.

The most important differentiator that Verizon may have up its sleeve is the acceleration of its 5G network deployment, which is currently not expected to be a reality until at least 2020. As the firm works to make its 5G network an actuality, it will continue to face an increasingly challenging operating environment. Recent weakness in subscriber additions could be foreshadowing a weaker revenue outlook for 2017, and it could force Verizon to look for inorganic growth prior to the launching of its 5G network, should management determine it is unable to continue enough positive momentum and maintain market share leading up to the network launch.

While the AT&T-Time Warner deal has the potential to transform the media and wireless telecom industries, it does little to impact our newsletter portfolios. At Valuentum, we tend to be debt-averse, and though we recognize the capital-intensive nature of the telecom industry, the mountain of debt needed to build and maintain proper infrastructure, the regulatory nature of the industry, as well as the free cash flow generating abilities of telecom giants like AT&T and Verizon, we aren't interested in adding exposure to an industry currently characterized by slowing growth and transformational mergers.

Though AT&T recently upped its quarterly dividend, we continue to be of the opinion that its best dividend growth years are behind it. Shares currently yield over 5.2%, which is sure to attract plenty of income-minded investors, but we are wary of what a substantial increase in debt will do to an already debt-heavy balance sheet. At last check, AT&T's Dividend Cushion ratio was below 0 as a direct result of such a lack of balance sheet health. We don't find Verizon's dividend any more attractive than AT&T's, even as it, too, continues to hike its quarterly payout. Verizon's shares yield ~4.8%, but the firm's Dividend Cushion ratio is also below 0 due to it holding just over $100 billion in net debt on its balance sheet. We recognize AT&T's strong free cash flow generation, and its net debt-to-adjusted EBITDA sat at 2.3x as of the end of the third quarter of 2016, but debt service costs, capital spending, and dividend obligations should not be underestimated by investors.

All things considered, the AT&T-Time Warner deal has captured our interest in the sense that it has the potential to further change the way we consume video content, but it has not captured our interest from an investment standpoint. Too much uncertainty on the regulatory front exists, as evidenced by the lack of favorable market reaction, and AT&T's lack of positive momentum following its DirecTV acquisition does not bode well for the integration of another massive acquisition. We're content with watching this story unfold from the sidelines. We're huge fans of the current selections already in the Dividend Growth Newsletter portfolio.

Cloud Lifting Microsoft Shares Toward All-Time Highs

By Kris Rosemann

Microsoft (MSFT) reported a strong quarter October 20, both in terms of financial performance and in terms of ongoing momentum in the transformation of its business. Non-GAAP revenue, which takes into account revenue deferrals from Windows 10, advanced just over 3% in the first quarter of fiscal 2017 thanks to a 6% revenue increase in 'Productivity and Business Processes' segment revenue and an 8% advance in 'Intelligent Cloud' segment revenue from the year-ago period. The firm's largest segment in terms of revenue, 'More Personal Computing,' reported a revenue decline of 2% on an as-reported basis.

Headlining the overall revenue growth for Microsoft was its Azure enterprise-grade cloud product suite more than doubling revenue from the first quarter of fiscal 2016; Azure's compute usage more than doubled in the quarter as well. Microsoft's Azure is now the most compliant cloud-based product line, with 49 certifications, more than any other cloud provider. Such a display of reliability has helped the firm advance its commercial cloud annualized revenue run-rate past the $13 billion mark and kept it on track to achieve its goal of reaching the $20 billion mark in fiscal 2018. In addition to the impressive growth of Azure, we love the double-digit growth we're seeing in server products and cloud services revenue, which is driven by attractive double-digit growth in annuity revenue.

Office 365--Microsoft's cloud-distributed, subscription-based productivity suite--continues to drive positive momentum in its 'Productivity and Business Processes' segment as Office 365 commercial revenue leapt more than 50% on a year-over-year basis. Office 365 consumer subscriber growth remained robust as well, growing to 24 million at the end of the first quarter of fiscal 2017 from 23.1 million in the fourth quarter of fiscal 2016 and 18.2 million in the first quarter of fiscal 2016.

While the non-GAAP numbers more appropriately highlight the momentum in Microsoft's business, in our opinion, GAAP figures do not show such a bright picture. GAAP revenue was roughly flat on a year-over-year basis, while GAAP operating income fell nearly 10%. Earnings per diluted share fell to $0.60 from $0.61 in the first quarter of fiscal 2016 despite a reduction of more than 200 million in diluted weighted average shares outstanding. Buybacks will continue as management works to close out a $40 billion repurchase program at the end of 2016, only to begin another $40 billion program after the year's end.

However, Microsoft flexed its free cash flow generating muscles in the first quarter of fiscal 2017. The software giant reported free cash flow of just under $9.4 billion, an increase of nearly 25% from the year-ago period despite capital expenditures jumping approximately 60%. Such strong free cash flow generation helped the firm advance its net cash position, excluding long-term equity and other investments of ~$10.5 billion, to an impressive $62.2 billion, up from $59.8 billion at the beginning of the quarter.

Microsoft's start to fiscal 2017 is a great display of what we love about the company. The momentum in its business transformation to a next-generation, cloud-based software company has been strong, and we love the higher-margin and recurring-revenue characteristics of a meaningful portion of its cloud business and what such visibility means for its ability to remain one of the most dynamic and dependable dividend ideas on the market today. On a related note, the firm has continued to generate significant amounts of free cash flow and maintained its balance sheet strength throughout its transformation. Further, we have little concern that management will neglect its shareholders in terms of cash returns, "Microsoft Remains Committed to Returning Capital to Shareholders."

Our position in Microsoft in the Dividend Growth Newsletter portfolio isn't going away anytime soon, even as shares continue to run ahead of our fair value estimate. We should make mention that at this point we are "playing with the house's money" after having taken significant profits in our outsize position in Microsoft in June 2016, "What?!?! Microsoft Acquires LinkedIn; NO!" The most recent quarter has done little to alter our opinion on the company, though we remain concerned about the impact the LinkedIn (LNKD) deal will have on its balance sheet and overall financial health both in the near term (in terms of a rising debt load) and over the long-run in terms of potential impairment charges down the road.

Please see *Cloud Lifting Microsoft…*on next page

*Cloud Lifting Microsoft...*from previous page

We continue to view Microsoft as one of the more attractive dividend payers on the market. Its dividend is fully funded by internal cash flow--unlike MLPs and REITs who are dependent on capital markets to maintain a competitive and growing distribution/dividend--and shares remain fairly valued unlike many high-PE consumer staples entities with similar payout yields and dividend growth histories. Microsoft currently yield ~2.7%. We continue to expect strong dividend growth at the company.

Pharma Momentum Builds for Johnson & Johnson

By Kris Rosemann

Best Ideas Newsletter portfolio and Dividend Growth Newsletter portfolio holding Johnson & Johnson's (JNJ) third quarter report October 18 was an impressive display of the success of its new product launches and the strength of its 'Pharmaceutical' business, which it expects is only just heating up. Johnson & Johnson is a long-time holding in the Dividend Growth Newsletter portfolio and was recently added to the Best Ideas Newsletter portfolio in January 2016 as a diversified pharma replacement for the more speculative Gilead (GILD). We see no reason to adjust our positions in Johnson & Johnson in either newsletter portfolio following the solid report.

Johnson & Johnson reported 4.2% sales growth on an as reported basis in the second quarter of 2016 from the comparable period in 2015 thanks to domestic sales growth of 6.7%. Excluding the impact of acquisitions, divestitures, and hepatitis C sales, on an operational basis, worldwide sales advanced nearly 6% from the year-ago period, while domestic sales jumped more than 7%. The firm's 'Pharmaceutical' business (~47% of total sales in the quarter) turned in sales growth of more than 9% as reported on a year-over-year basis as strength in domestic sales (nearly 12% growth) led the segment higher. The company's 'Consumer' and 'Medical Devices' segments reported sales increases of 1.6% and 1.1%, respectively, from the third quarter of 2015.

Strong execution coupled with solid top-line expansion resulted in notable bottom-line performance for J&J. Adjusted diluted earnings per share increased nearly 13% to $1.68 after accounting for one-time items in the quarter and the comparable period of 2015. Management raised its adjusted earnings per share guidance for 2016 yet again; it has increased its earnings guidance range after each quarter thus far in the year. It now anticipates adjusted earnings per share to be in a range of $6.68-$6.73, compared to initial guidance of $6.43-$6.58 issued in January 2016. We like the earnings momentum.

Johnson & Johnson's 'Pharmaceutical' business is the engine behind its growing performance expectations, and it continues to deliver on expectations set out in its latest business review in May 2015. Branded products continue to turn in impressive results and solid volume gains, while additional volume growth and opportunities for line-extensions are prevalent in all core therapy areas. Since May 2015, the firm has filed or gained approval for 16 meaningful line extensions. It believes it has 10 potential line extension filings lined up with $500+ million in individual sales potential, including for established drugs such as Simponi, Stelara, and Xarelto. The company has also launched the first of 10 new molecular entities (NMEs) in its pipeline with $1+ billion individual sales potential, has filed another for approval, and plans to file another by year end. All 10 NMEs are expected to be filed by 2019.

Johnson & Johnson's pharmaceutical portfolio is already one of the strongest on the market, and its pipeline is poised to, at the very least, continue its impressive performance. Oncology continues to be a highlight across the pharmaceutical industry, "Oncology News a Key Driver of Big Pharma (August 2016)" and J&J has heavy exposure to the oncology market--it turned in $1.5 billion in revenue on ~30% sales growth in the third quarter of 2016 in oncology--and expects to continue growing its treatments in the area in part via meaningful line extension filings for Imbruvica. Because of such filings, the firm is confident in its growth prospects through 2019 despite material competition from a growing number of biosimilars entering the market and increasing regulatory scrutiny, particularly on industry-wide pricing practices. The company's 'Consumer' business still boasts a portfolio of well-recognized, steady-performing consumer

Please see *Pharma Momentum Builds...*on next page

Pharma Momentum Builds…from previous page

brands, and its 'Medical Devices' segment stands to benefit from the recent acquisition agreement for Abbott's (ABT) 'Medical Optics' business. The clear driver of Johnson & Johnson's outperformance, however, is its impressive 'Pharmaceutical' business.

Compound	Current Phase	Anticipated Filing Date
IMBRUVICA® CLL 2nd Line	Approved 2016	2015
STELARA® Crohn's disease	Approved 2016	2015
DARZALEX® Relapsed refractory MM	Registration Filed	2016
Darunavir HIV STR with C/F/TAF	Registration Filed^	2016
EDURANT® HIV single tablet regimen with dolutegravir	Phase 3	2017
DARZALEX® Frontline MM (non-transplant)	Phase 3	2018
IMBRUVICA® Diffuse large B cell Lymphoma frontline combo	Phase 3	2018
IMBRUVICA® Follicular lymphoma relapsed/refractory	Phase 3	2018
IMBRUVICA® CLL (young/fit) frontline combination	Phase 3	2019
DARZALEX® Frontline MM (transplant)	Phase 3	2019

Image above: Johnson & Johnson's planned line extension filings, each with $500+ million sales potential. Source: J&J presentation

Compound	Current Phase	Anticipated Filing Date
DARZALEX® Multiple myeloma double refractory	Approved 2015	2015
Sirukumab Rheumatoid arthritis	Registration Filed	2016
Guselkumab Psoriasis	Phase 3	2016
Apalutamide (ARN-509) Pre-metastatic prostate cancer	Phase 3	2017
Erdafitinib (FGFR inhibitor) Solid tumors	Phase 2	2018
Esketamine Treatment-resistant depression	Phase 3	2018
Imetelstat Myelofibrosis	Phase 2	2018
JNJ-1575 (AL-8176) Respiratory syncytial virus	Phase 2	2019
JNJ-4178 (3DAA) Hepatitis C virus	Phase 2	2019
JNJ-3872 (VX-787) Influenza	Phase 2	2019
JNJ-7922 (Orexin-2 antagonist) Primary insomnia	Phase 2	2019

Image above Johnson & Johnson's planned NME filings, each with $1+ billion sales potential. Source: J&J presentation

All in, we're still huge fans of Johnson & Johnson. At the time of this writing, the company's shares yield ~2.7%, which mirrors its impressive Dividend Cushion ratio of 2.7. In addition to Johnson & Johnson's competitive dividend, we like the chances for shares to appreciate toward the upper bound of our fair value estimate, particularly given the levels at which other strong dividend-paying entities are trading in the current market environment and the company's impressive pharmaceutical portfolio and pipeline. Hey what do you say – we like J&J!

Hasbro Heads into Holiday Season with Record Quarter

By Kris Rosemann

Dividend Growth Newsletter portfolio holding Hasbro (HAS) reported one of the most successful quarters in company history October 17. The firm registered company records in quarterly revenue and earnings as each of its major operating segments generated sales growth. US and Canada revenue advanced 16% on a year-over-year basis in the quarter, while International revenue increased 13%. Its Entertainment and Licensing segment hopes to continue building momentum as revenue grew 8% from the year-ago period, which helped the company to record quarterly sales of nearly $1.7 billion. We like Hasbro a lot.

Strength in Europe and Latin America helped Hasbro's International segment overcome relative weakness in the Asia Pacific region, but the highlight of the firm's portfolio was its performance in the 'Girls' product category, where revenue leapt 57% in the quarter and 48% in the first nine months of 2016 on a year-over-year basis. The Disney (DIS) Princess and Frozen product lines remain the core drivers of such strong performance, with ancillary growth coming from the Dreamworks' Trolls as well as the Baby Alive and Furby product lines. Hasbro continues to show its recent dominance over Barbie-maker Mattel (MAT) as things are beginning to gear up for the holiday season, which is more often than not the make or break quarter for both firms in any given year.

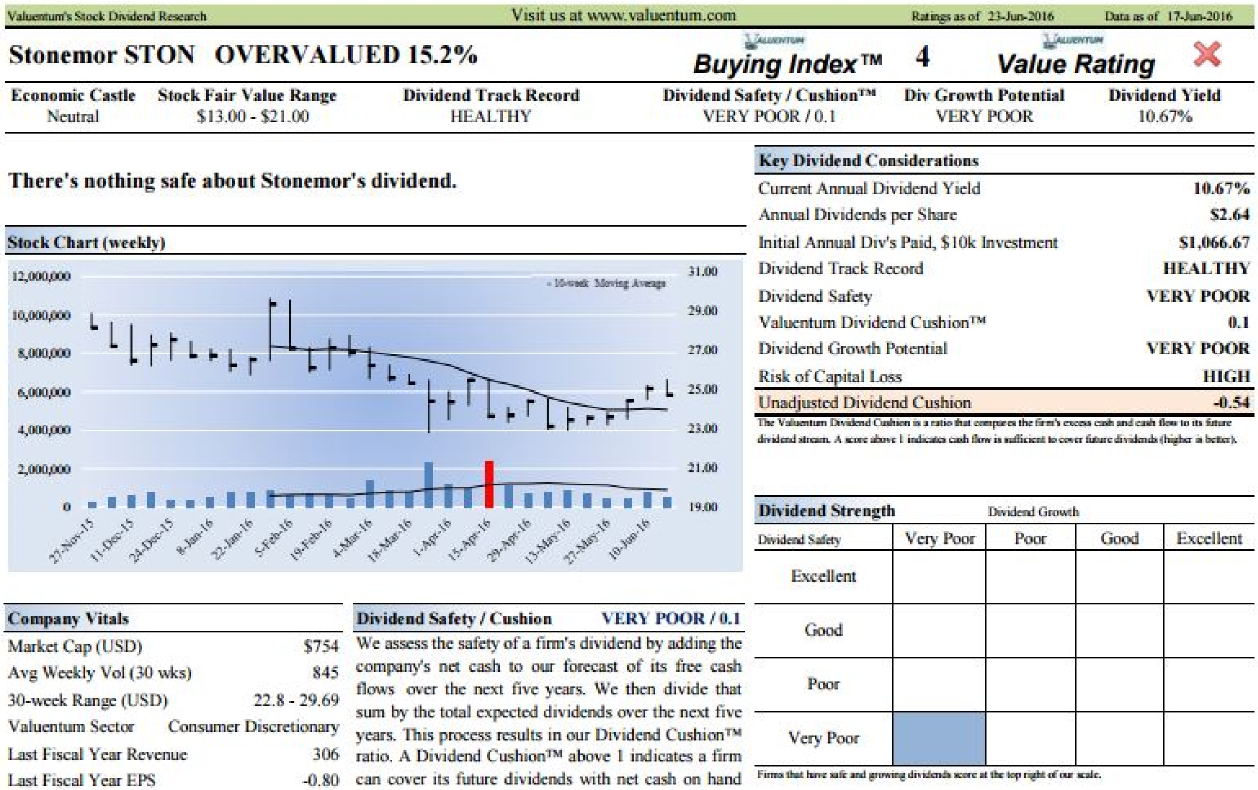
However, the impressive top-line performance was not the only noteworthy aspect of Hasbro's third quarter report. The firm improved operating profit margin by a full percentage point from the comparable period in 2015 to 21.6% thanks in part to improvements in cost of sales, advertising spending, and product development costs. Earnings per diluted share jumped nearly 24% on a year-over-year basis in the quarter as well, and its record-setting bottom line made its presence felt on the cash flow statement. Free cash flow generation came in at more than $50 million for the first nine months of 2016, up considerably from negative $28 million in the same period of 2015. Weak free cash flow prior to the peak holiday sales season is not uncommon for a firm so dependent on the holiday season like Hasbro.

Despite the fact that its most important quarter is only a few weeks underway, we love what we're seeing from Hasbro thus far in 2016. The firm's solid cash flow performance in recent periods has helped its balance sheet health, while elevating its quarterly payout earlier this year, "Dividend Giant Hasbro Surges; Raises Dividend 10%+." Since the end of the third quarter of 2015, Hasbro has improved its net debt position to ~$718 million from ~$996 million. We're expecting the company to build on its impressive performance through the first three quarters of the year as we get into the most important, and most profitable, season of the year. Consumer spending, particularly in the US, has been an area of uncertainty as of late, driven by concerning trends in retail and restaurants, but Hasbro's impressive performance in recent periods is a sign that consumers are still willing to give children what they want, even if traditional spending habits are changing.

It's important to keep context when evaluating our position in the firm, as shares have pulled back from recent highs in the upper $80s but have far more than doubled since their addition to the Dividend Growth Newsletter portfolio at less than $32 in late 2011. Recent investor concern over the pace of growth in its 'Boys' product category seems to have been masked by exuberance over the tremendous performance of Hasbro's 'Girls' products. We love the momentum we're seeing within the firm's business as it heads into the holiday season. We're more than happy to continue letting this big winner run and think the firm's shares have the potential to reach the high end of our fair value range, the upper $80s. Throw in a strong dividend yield of ~2.7% at recent price levels coupled and a solid Dividend Cushion ratio of 1.7, and the case for Hasbro's inclusion in the Dividend Growth Newsletter portfolio is a good one.

As Expected--MLP StoneMor Partners Slashes Distribution!

By Brian Nelson, CFA


Valuentum's Stock Dividend Research | Visit us at www.valuentum.com | Ratings as of 23-Jun-2016 | Data as of 17-Jun-2016

Stonemor STON OVERVALUED 15.2% | Buying Index™ 4 | Value Rating ✗

Economic Castle	Stock Fair Value Range	Dividend Track Record	Dividend Safety / Cushion™	Div Growth Potential	Dividend Yield
Neutral	$13.00 - $21.00	HEALTHY	VERY POOR / 0.1	VERY POOR	10.67%

There's nothing safe about Stonemor's dividend.

Key Dividend Considerations	
Current Annual Dividend Yield	10.67%
Annual Dividends per Share	$2.64
Initial Annual Div's Paid, $10k Investment	$1,066.67
Dividend Track Record	HEALTHY
Dividend Safety	VERY POOR
Valuentum Dividend Cushion™	0.1
Dividend Growth Potential	VERY POOR
Risk of Capital Loss	HIGH
Unadjusted Dividend Cushion	-0.54

The Valuentum Dividend Cushion is a ratio that compares the firm's excess cash and cash flow to its future dividend stream. A score above 1 indicates cash flow is sufficient to cover future dividends (higher is better).

Stock Chart (weekly)

Company Vitals	
Market Cap (USD)	$754
Avg Weekly Vol (30 wks)	845
30-week Range (USD)	22.8 - 29.69
Valuentum Sector	Consumer Discretionary
Last Fiscal Year Revenue	306
Last Fiscal Year EPS	-0.80

Dividend Safety / Cushion VERY POOR / 0.1

We assess the safety of a firm's dividend by adding the company's net cash to our forecast of its free cash flows over the next five years. We then divide that sum by the total expected dividends over the next five years. This process results in our Dividend Cushion™ ratio. A Dividend Cushion™ above 1 indicates a firm can cover its future dividends with net cash on hand

Dividend Strength

Dividend Safety \ Dividend Growth	Very Poor	Poor	Good	Excellent
Excellent				
Good				
Poor				
Very Poor	■			

Firms that have safe and growing dividends score at the top right of our scale.

Image: A clipping of Valuentum's dividend report on StoneMor Partners.

We continue to defend the individual investor!

StoneMor Partners (STON) is about the most risky entity in all of our coverage universe, and it showed why after the trading session, October 27, by cutting its distribution! Yes, yet another MLP! For those that listened to us about the severe risks of its business model, we salute you. The MLP has been what we call a double whammy--it's on Valuentum's most overvalued list here → (http://www.valuentum.com/articles/20130220_2), and it had a Dividend Cushion ratio of 0.1, now -0.7 (anything less than 1 is risky, but close to or below 0 implies significantly heightened risk). Shares are indicated down 25% after the close October 27.

Before going further, I am pleading with you. If you are still reading free research and analysis, which told you that StoneMor's dividend was okay (or is included in some "model" portfolio), I am begging you to stop reading the source of the work…for your own sake. You know that we continue to exceed the benchmark performance in the respective newsletters, and our efforts to help the income investor have been second to none! *We are a paid service for a reason!* It showed why in an absolutely huge way today.

Okay – enough of my pleas. Here's what we said about StoneMor's distribution in its Dividend Report:

> <u>Key Strengths</u>
>
> There's nothing that any bullish (optimistic) holder of Stonemor's units could ever say to make us feel comfortable with an investment in the MLP. Its free cash flow is insufficient, and its balance sheet is "buried" under a significant amount of debt. The MLP is incredibly capital-market dependent and has used the issuance of new units (equity) to fund operating cash flow shortfalls to keep its distribution "alive." In the past three years alone, Stonemor has issued ~$290 million in

Please see *As Expected…*on next page

As Expected...from previous page

new equity (dilution). The company's personal care trust funds are tied to market activity, and its pre-need business causes severe business cash-flow imbalances. Stonemor's distribution may not make it through the most difficult times.

Potential Weaknesses

We're going to call it how it is: Stonemor's distribution is far from safe. The master limited partnership (MLP) business model is one that we're not particularly fond of, and while some investors are comfortable with the term distributable cash flow, we are not. We prefer the traditional measure of free cash flow when evaluating the health of a payout, and Stonemor's cumulative free cash flow generation during the past three years (2013-2015) of ~$5.3 million is a mere fraction of its cash distributions paid over the same time period ($190+ million). Long-term debt of ~$640 million relative to a negligible cash balance of $15 million should send income investors running for cover. We'd be scared "to death" holding Stonemor for income purposes.

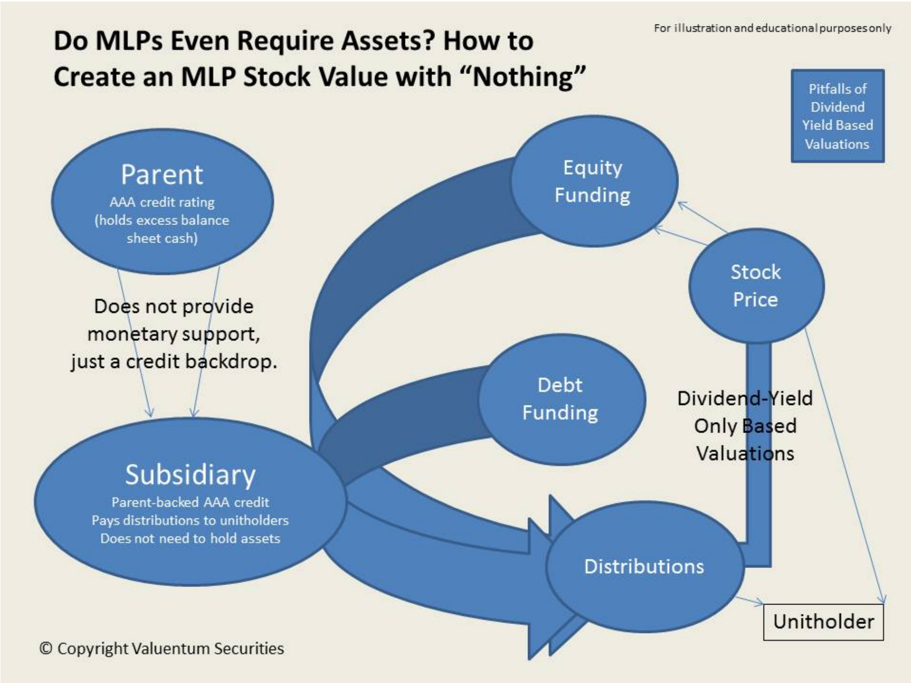
When a company's or MLP's Dividend Cushion ratio flashes a dangerous signal, my goodness, please take it seriously. It doesn't guarantee disaster, but it spells significantly heightened risk given that the entity simply doesn't have a lot of cushion to work to cover the payout. In StoneMor's case, it didn't have the capital it needed to support revenue initiatives, and therefore had to use cash that otherwise had been going to unitholders to do so. Our fair value estimate for StoneMor was $17 per share prior to the share-price collapse (now the fair value is $11). By the way, check out page 3 of the March 2016 Dividend Growth Newsletter here (http://www.valuentum.com/downloads/20160301_1/download) – "StoneMor's Shares Are Gravely Overpriced." You can download StoneMor's full report here (http://www.valuentum.com/downloads/20120308_5/download).

Please let us help! In order to make sure your membership is current, please contact us at info@valuentum.com. **Don't let free research and analysis cost you dearly!** We'll be here for you. Valuentum isn't going anywhere. We got yet another one spot on.

Article updated following release of Valuentum's updated reports on StoneMor. Includes new fair value estimate and Dividend Cushion ratio.

Are MLP Structures Phony?

By Brian Nelson, CFA



Please see *Are MLP Structures*...on next page

*Are MLP Structures...*from previous page

Using a hypothetical example of an MLP and its parent, let's explain how MLP stock value can essentially be created from "nothing." The following example is purely hypothetical and for educational purposes only.

Let's say the parent holds a pristine AAA credit rating backed by its own strong, recurring free cash flow generation and asset base. In order to put its excess cash to use, the parent decides to create a new MLP subsidiary and pledges to provide financial support to the entity.

The parent also pledges that it will provide a growing stream of cash flows through the subsidiary that can be used as distributions from the subsidiary to the subsidiary's unitholders. This is only a pledge though. No money will actually be transferred from the parent to the subsidiary.

The parent also guarantees the subsidiary's distribution stream and any and all of the subsidiary's debts, thereby giving the subsidiary an investment-grade credit rating. With its investment-grade credit rating, the subsidiary borrows heavily against the "pledged" future cash flow stream (collateral) that is implicitly backed the parent (sourced from the parent).

The subsidiary then uses the newly-raised debt to backstop its very own future distribution payments to its very own future unitholders. With the newly-raised debt alone, the subsidiary, for example, could be able to cover growing distributions to its future unitholders for years depending on the growth rate, with the pledged capital from the parent no longer required.

The parent now takes the subsidiary public.

The subsidiary now raises equity on the open market such that, when combined with its newly-raised debt, it is now able to fund its entire growing dividend stream on a go-forward basis via external capital-raising efforts, maybe on a 50%/50% equity/debt split if it wants to. In other words, the subsidiary can fund its entire future and growing dividend stream purely from financing activities with nothing from the parent at all (or even no assets!).

Since there is no minimum distributable-cash-flow to distributions-paid mandate (as in the case of most MLP arrangements), the parent would only have to stand as a backdrop and guarantee the newly-created entity's future distributions and debt load. The external financing markets are sustaining the subsidiary's dividend, and yield-based valuation approaches prop up the subsidiary's stock price.

What the parent has done in this example is financially engineer the future distribution stream and capital structure of a brand new distribution-paying entity with effectively no new capital or assets at all. The parent is just standing behind the subsidiary reinforcing its investment-grade borrowing capacity, which supports the distribution that supports the equity price, which provides incremental equity capital that can also be used to support the distribution and so on.

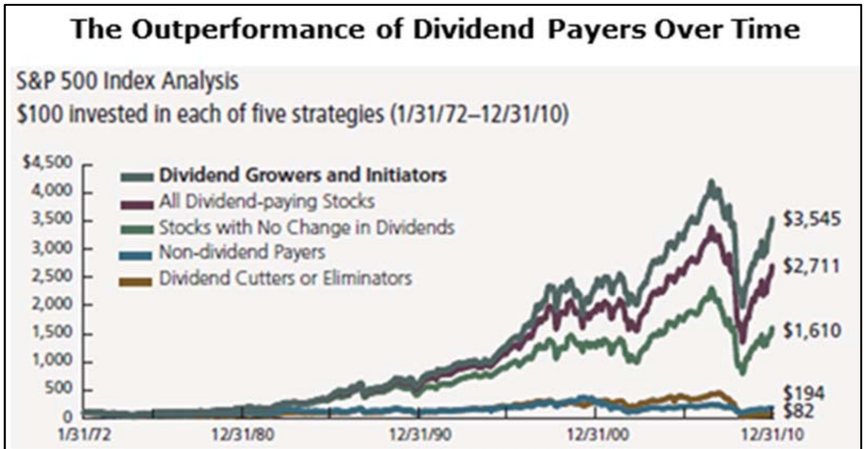
One may even say that there's nothing to stop the parent from conducting more arrangements like this many times over. It's possible that a parent can create trillions of equity market capitalization by just creating these new dividend-paying subsidiaries over and over again. The parent's balance sheet and cash flow generation are assets much like the pipelines in the ground are assets -- so there is tangible backing.

Obviously, there is a very good reason, in our view, why dividends should be paid out of traditional free cash flow (cash from operations less all capital spending) or earnings, as anything else is textbook financial engineering (and holds no value). The moral of this story: We're sticking with companies that have organically-derived dividends, ones that are actually paid out of traditional measures of free cash flow, not the MLP industry's measure of distributable cash flow, which we believe is in part funded through equity and debt issuance.

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.

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

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 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) Forecasts 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 11

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 18: http://files.shareholder.com/downloads/JNJ/3045880264x0x911936/1C9F81CC-F55B-4FA5-A7B3-0D991B055AF6/JNJ_Earnings_Presentation_3Q2016.pdf

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

© Valuentum Securities