OUR DIVIDEND GROWTH NEWSLETTER

Valuentum Securities

Stock Analysis: From Value through Momentum Investing

February 1, 2017
Volume 6 Issue 2

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

Latest Alerts: We added CVS Health (CVS), Boeing (BA), Hanesbrands (HBI), and the Alerian MLP ETF (AMLP). See portfolio on page 5.

Annualized Return	Annualized Goal	Outperformance
11.8%	Mid-High Single Digits	4.3pts

*Please see note below regarding performance measurement.

Inside This Issue

1 How Sweet It Is (To Be An Apple Shareholder)
2 Apple Reports Record Quarterly Results in Return to Top-Line Growth
3 Coach's Fundamentals Improving But We're Growing Concerned About Dividend Amid Rumored M&A Talks
4 Exxon Mobil Still Battling Back
5 The Dividend Growth Portfolio
6 Consumer Staples: Product Pricing Gains To Wane in 2017?
8 Novartis' Continuous Dividend Growth and Promising Pipeline
10 Stocks with High Valuentum Buying Index Ratings and Strong Dividend Growth Prospects
11 The Financially-Healthiest Dividend Payers Yielding Over 2%
12 Yields to Avoid
16 AT&T's Love Affair with Debt
17 Boeing's Lift Off, Lockheed's Caution, and United Tech's Outlook
19 Adding an Undervalued, Dividend Growth Prospect
20 Addressing the Intricacies of the Dividend Cushion Ratio
22 About the Dividend Cushion™ Ratio

"Apple has been a staple of both newsletter portfolios for years, and it's just hard to miss our glowing reviews of the company's competitive advantages, free cash flow generating prowess, and net balance sheet strength."
– Brian Nelson, CFA

Latest Changes

CVS Health:
http://www.valuentum.com/articles/CVS_Health_In_The_Bargain_Bin_We_Think_So

1/26 Transactions:
http://www.valuentum.com/articles/Alert_Trading_MLPs_Adding_Boeing_Adding_Hanesbrands

How Sweet It Is (To Be An Apple Shareholder)

By Brian Nelson, CFA

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

Kris Rosemann
Associate Investment Analyst
kris@valuentum.com

Alexander J. Poulos
Healthcare & Biotech Contributor

Dividend Growth Ideas: MO, AAPL, AMLP, BA, CBRL, COH, CSCO, CVS, XLE, GE, GM, HAS, HBI, 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, February 1, 2017, the portfolio is significantly exceeding this goal.

Apple (AAPL) shareholders may have been singing this rendition of Marvin Gaye's 1964 classic "How Sweet It Is (To Be An Apple Shareholder)." Apple has been a staple of both newsletter portfolios for years, and it's just hard to miss our glowing reviews of the company's competitive advantages, free cash flow generating prowess, and net balance sheet strength. On Wednesday, February 1, the date of the publishing of this newsletter, shares of Apple closed at nearly $129, just shy of its all-time high. *How sweet it is… indeed!* Page 2 is dedicated to the company's most recent quarterly report, so please have a read.

We have a jam-packed newsletter this month. But first, you have to know that we added CVS Health (CVS), Boeing (BA), Hanesbrands (HBI) and the Alerian MLP ETF (AMLP) to the Dividend Growth Newsletter portfolio since the release of previous edition in January. For those that may have missed our emails, we cover the rationale behind those new additions on pages 17-19. Just a reminder, unlike the Best Ideas Newsletter portfolio, within the Dividend Growth Newsletter portfolio, we may relax certain valuation considerations to achieve targeted portfolio goals -- and to reiterate, the Alerian MLP ETF addition should be viewed as a "trade," not an investment consideration. We continue to be very cautious on the long-term sustainability of the MLP business model.

Some of you may have already read our work on Novartis (NVS) and AT&T (T), but we've included our thoughts on them in this newsletter edition, too. We're strongly considering the former, but are starting to get worried about the latter's "love affair with debt." The same holds true for Verizon. There's tons of new content in this newsletter edition you haven't seen before either. We have growing concerns about the dividend health of Coach (COH), which we outline on page 3, you can learn about free cash flow in the context of Exxon Mobil (XOM) on page 4, and on page 6, you can survey our thoughts on the product pricing environment of a couple consumer staples entities. We still include Procter & Gamble (PG) in the Dividend Growth Newsletter portfolio.

Our writings aren't all rosy though. We have the standard 'Dividend Yields to Avoid List' on page 12, and to really get to know the Dividend Cushion ratio, you have to get familiar with situations where it goes wrong on page 20. It's a wonderful tool, but it's not perfect. The more that you know about it, the more powerful of a tool it becomes! Understanding how and why the Dividend Cushion ratio is put together is sometimes as important as the ratio itself. With all of that said, I sincerely hope that you enjoy this February edition of the Dividend Growth Newsletter!

Apple Reports Record Quarterly Results in Return to Top-Line Growth

By Kris Rosemann

On January 27, tech giant and newsletter portfolios holding Apple (AAPL) reported the highest quarterly revenue in its history in the first quarter of its fiscal 2017, along with all-time unit and revenue records for the iPhone and Apple Watch, all-time records for its 'Services' segment revenue and Mac sales, and all-time revenue records for four of its five geographic segments despite considerable currency headwinds. Such impressive top-line performance across the board helped drive record quarterly earnings per share as well.

We recently increased our fair value estimate for shares of Apple to $159 after reassessing our near-term top-line growth expectations, which we expect to be in the mid-single digit range, suggesting shares are still attractively priced on a discounted cash flow basis. Though its dividend yield is not among the most compelling on the market, the company's dividend growth potential and dividend safety are among the best in our coverage universe thanks to its fortress-like balance sheet that continues to build with each passing quarter of robust free cash flow generation. All of these qualities are reflected in its astounding Dividend Cushion ratio of 5 at last check. We're not letting go of shares anytime soon.

Apple's headliner clearly remains the iPhone, and the most recent quarter saw iPhone demand surpass management's expectations, a welcome report after a slight blip in sales in fiscal 2016. The Mac was able to buck global PC market trends and return to revenue and unit growth on a year-over-year basis in the quarter ended December 31, albeit slightly, on its way to record quarterly revenue, speaking to Apple's brand strength. Apple's leading position in the wearable technology market is further evidence of its combination of brand power and innovative nature, as holiday demand for the Apple Watch, the world's best-selling smartwatch, surpassed supply.

We continue to point to Apple's ecosystem as a key competitive advantage beyond the allure of its hardware, and it enables Apple to be 'with' consumers at the gym, on the go, in their homes, and at work. The firm is also beginning to gain momentum with enterprise level customers looking to connect mobilized workforces more efficiently. December 2016 was the App Store's best month ever in terms of purchases, and the company's 'Services' segment is only beginning to gain steam, according to management. It expects the segment to be the size of a Fortune 100 company this year, and its goal is to double the size of the business in the next four years. Apple appears well on its way to achieving that goal, as the number of people transacting on its stores is increasing at a strong double-digit rate in addition to average revenue per paying customer growing at a double-digit pace.

We love what the doubling of the higher-margin 'Services' segment would mean for Apple's overall profitability levels, and the increasingly subscription-based sales model provides additional visibility into the business. The tech giant doesn't need a boost when it comes to dividend growth potential--free cash flow in the most recent quarter came in at ~$23.7 billion compared to cash dividends paid of ~$3.1 billion--but the characteristics of its expanding 'Services' business are some that we associate with top income ideas. Better than company-average margins, low capital intensity, and a predictable and growing revenue stream all play directly into the dividend growth investor's hand.

Shares of Apple are changing hands at less than 14.4 times fiscal 2017 consensus earnings estimates as of this writing, or just below the lower bound of our fair value range, and we plan to continue to include shares in the newsletter portfolios for the foreseeable future. We may consider making our position in the Dividend Growth Newsletter a full 5% weighting sometime in the near future as we continue to look for uses of our sizeable cash balance in the portfolio. The decision to add to our current position may ultimately rest on how the board handles the potential for a dividend increase this spring, as it has hiked the quarterly payout each spring since 2012. Shares yield ~1.8% as of this writing, a bit light when considering the objectives of the Dividend Growth Newsletter portfolio, but the potential for dividend payments to multiply from current levels and still be covered by free cash flow generation is certainly an enticing proposition, particularly when coupled with Apple's current valuation profile.

Coach's Fundamentals Improving But We're Growing Concerned About Dividend Amid Rumored M&A Talks

By Kris Rosemann

We've been keeping a close eye on the speculative luxury goods ideas in the newsletter portfolios, and it hasn't all been smooth sailing as Coach (COH) and Michael Kors (KORS) work to reposition their brands in the North American markets. Though we continue to see an opportunity for capital appreciation in shares of Coach (based on our fair value estimate of $41 per share), which is yielding ~3.7% at recent price levels, we're growing concerned about the implications that M&A (if rumors come to fruition) will have on the long-term health of the dividend. Many, for example, are speculating Coach may purchase Kate Spade (KATE), while others have reported that Coach had been in talks with Burberry (BURBY). For now, however, Coach's near-term free cash flow generating capacity and net cash position on the balance sheet are just good enough to keep it in the Dividend Growth Newsletter portfolio. The handbag maker's Dividend Cushion ratio stands at 1.9, but a foolish debt-funded acquisition could alter the strength of the payout in a heartbeat. We're not as comfortable with shares as we once were, prior to the Stuart Weitzman purchase, which absorbed a considerable amount of its net cash.

Nevertheless, Coach's fiscal 2017 second quarter report, released January 31, suggests recent rebranding tactics may be bearing fruit. The company reported that net sales advanced 4% in the second quarter of fiscal 2017 from the year-ago period despite management's estimate that reported sales were negatively impacted 1% from the strategic decision to reduce promotional events and close stores in the North American wholesale channel. The repositioning was not enough to keep the Coach brand from beating expectations for comparable sales in North America either, as it turned in 3% growth on a year-over-year basis compared to consensus estimates of 2.4% growth in the period. Coach delivered double-digit earnings per diluted share growth in the fiscal second quarter as well, as more than a one percentage point expansion in gross margin helped diluted earnings per share jump to $0.71 from $0.61 in the year-ago period. The reduction in North America Coach brand promotional activity helped support the bottom-line performance.

Though Coach will bring on board a new CFO in March (Kevin G. Willis), the executive team appears to be doing a lot of things right, as of late, in the midst of a very challenging retail environment. For example, a recent read into average spend per consumer on handbags suggests aspirational goods makers avoiding promotional activity is a sound strategy, as while the number of handbags purchased per consumer has been flat during the past three years, the average spend per consumer on handbags on a trailing twelve month basis has grown each year since 2014. Rival luxury brand firm LVMH (LVMHF), who is battling the ultra-aggressive discounting in retail by avoiding the listing of its products on Amazon's (AMZN) online selling platform, also reported a strong finish to calendar 2016 January 26 as its revenue jumped 9% from the fourth quarter of 2015. Holding the line with price to maintain solid brand positioning looks like the best way to navigate the tumultuous environment.

Looking ahead, Coach reduced its fiscal 2017 revenue guidance in the quarterly release due to increased expectations for currency exchange headwinds. Management now expects revenue to grow at a low-single digit rate, compared to previous expectations for a low-to-mid-single digit increase. Coach still anticipates a double-digit growth rate in both net income and earnings per diluted share in the full fiscal year. We like the targets, and while the robust bottom-line expansion bodes well for the objectives of the income-oriented Dividend Growth Newsletter portfolio, we can't rule out the possibility of potentially foolish M&A with Coach on the buying side of the negotiations table. Coach is doing a lot of things right operationally, but with shares now trading above average cost, even excluding dividends, the time may be ripe for us to rid the Dividend Growth Newsletter portfolio of this speculative position. The potential for further capital appreciation may not be worth the added risk of a dividend cut that may come with M&A activity, particularly in the context of the Dividend Growth Newsletter portfolio. Stay tuned.

Exxon Mobil Still Battling Back

By Kris Rosemann

In light of the well-publicized recent dividend cuts at ConocoPhillips (COP) and Kinder Morgan (KMI), it's no surprise to readers why we continue to prefer the diversified Energy Select SPDR ETF (XLE) when it comes to energy exposure in the newsletter portfolios. Operating debt-heavy, capital-intensive business models in a violently cyclical industry such as upstream exploration and production can be a recipe for disaster, as the fallout of 2015 showed. Exxon Mobil (XOM), however, continues to be one of our favorite income ideas relative to its energy peers, and it only makes sense that Exxon Mobil also makes up more than 16% of the XLE, too. It also benefits from having both upstream and downstream assets.

What's more, during 2016, Exxon Mobil was significantly free cash flow positive on an annual basis, as measured by cash flow from operations less all capital spending, something that cannot be said for all of its rivals. As performance has rebounded along with oil prices in recent quarters, traditional free cash flow alone is still coming up short in covering cash dividends paid though. As the image below shows, Exxon Mobil has to consider proceeds from asset sales and capital market issuance to meet both capital spending and dividend obligations. Expectations for continued improvement in energy resource prices in the coming years helps to push the company's Dividend Cushion near parity, however, offsetting near term shortfalls.

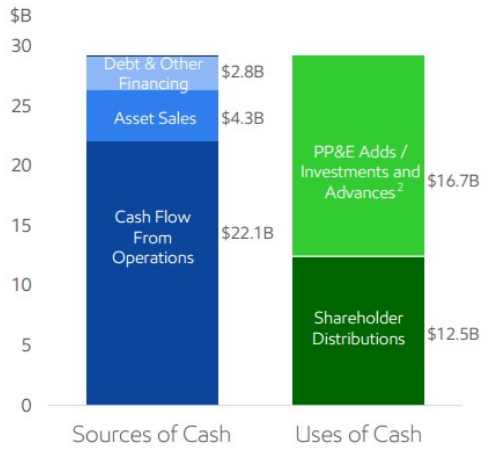


Image Source: Exxon Mobil fourth quarter presentation

The fourth quarter of 2016 was a sign of things moving in the right direction for Exxon, but free cash flow generation in the period of $2.6 billion ($7.4 billion in cash flow from operations less $4.8 billion in capital and exploration expenditures = $2.6 billion in free cash flow) still came up short in covering cash dividends paid in the quarter ($3.1 billion). Only when proceeds from asset sales ($2.1 billion) are included in the calculation are dividends then covered. This is an improvement over full-year results, where the company had to access the debt/equity markets to fund free cash flow and asset-sale shortfalls, but still insufficient organic quarterly performance, nonetheless.

Asset sales are not included in traditional definitions of free cash flow because they are not sustainable operationally (a company, for example, cannot continue to sell its assets forever, and therefore such sales are excluded from traditional free cash flow). Still, traditional free cash flow is trending in the right direction at Exxon thanks to material reductions in capital spending (down 35% in the fourth quarter and 38% on a year-over-year basis in 2016) and rebounding commodity prices, which are aiding operating cash flow improvements (up 70%+ in the fourth quarter, but still down meaningfully on a full-year basis).

Perhaps most importantly, Exxon Mobil did a good job preserving its balance sheet throughout a difficult 2016. Management was able to fund all of its business needs as well as $12.5 billion in shareholder distributions in the year with only ~$2.8 billion in incremental debt and other financing. This compares favorably to the likes of Chevron (CVX), whose total debt load, for example, rose nearly $8 billion in the year. Exxon is anticipating a return to growth in capital spending in 2017, up to $22 billion from $19.3

Please see *Exxon Mobil*...on page 6

The Dividend Growth Portfolio

Annualized Return	Annualized Goal	Outperformance
11.8%	Mid-High Single Digits	4.3pts

The Dividend Growth Newsletter portfolio has advanced 76.6% since inception, January 2012.

DIVIDEND GROWTH PORTFOLIO -- as of February 1, 2017 — 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	71.39	7,210.39	4.1%	246.44
Apple (AAPL)	7/24/2013	63.17	51	3,228.45	128.75	6,566.25	3.7%	116.28
Alerian MLP ETF (AMLP) New	1/26/2017	13.19	398	5,256.62	13.19	5,249.62	3.0%	382.08
Boeing (BA) New	1/26/2017	168.44	31	5,228.64	163.97	5,083.07	2.9%	176.08
Cisco (CSCO)	11/14/2014	26.31	199	5,242.53	30.49	6,067.51	3.4%	206.96
Coach (COH)	9/19/2014	37.55	80	3,011.00	37.81	3,024.80	1.7%	108.00
Cracker Barrel (CBRL)	2/1/2016	133.50	18	2,410.00	156.86	2,823.48	1.6%	82.80
CVS Health (CVS) New	1/6/2017	81.84	107	8,763.88	77.97	8,342.79	4.7%	214.00
Energy Sector SPDR (XLE)	4/1/2015	72.63	121	8,795.76	72.36	8,755.56	5.0%	232.90
General Electric (GE)	10/21/2013	26.18	240	6,290.20	29.69	7,125.60	4.0%	230.40
General Motors (GM)	12/1/2016	36.43	119	4,342.17	36.14	4,300.66	2.4%	180.88
Hasbro (HAS)	12/30/2011	31.89	110	3,514.90	82.13	9,034.30	5.1%	224.40
Hanesbrands (HBI) New	1/26/2017	23.77	221	5,260.17	23.23	5,133.83	2.9%	132.60
Intel (INTC)	12/30/2011	24.25	289	7,015.25	36.52	10,554.28	6.0%	300.56
Johnson & Johnson (JNJ)	12/30/2011	65.58	107	7,024.06	113.23	12,115.61	6.9%	342.40
Medtronic (MDT)	12/30/2011	38.25	78	2,990.50	76.00	5,928.00	3.4%	134.16
Microsoft (MSFT)	12/30/2011	25.96	77	2,005.92	63.58	4,895.66	2.8%	120.12
Proctor & Gamble (PG)	12/30/2011	66.71	105	7,011.55	87.33	9,169.65	5.2%	281.40
PP&L (PPL)	12/30/2011	29.42	238	7,008.96	34.95	8,318.10	4.7%	361.76
Realty Income (O)	7/24/2013	44.35	60	2,668.00	58.31	3,498.60	2.0%	151.80
S&P Dividend ETF SPDR (SDY)	4/20/2016	81.33	105	8,546.65	85.56	8,983.80	5.1%	223.70
Vanguard REIT ETF (VNQ)	2/1/2016	77.07	32	2,473.24	81.38	2,604.16	1.5%	94.79
Latest Changes: Added CVS (1/6/2017); Added BA (1/26/2017); Added HBI (1/26/2017); Added AMLP (1/26/2017).								
Cash -- changes in cash balance reflects dividends received and trading gains/losses, where applicable						31,824.42	18.0%	4,544.51
Dividend Growth Portfolio				100,000.00		**176,610.14**	100.0%	**TBD**
DG Portfolio Annualized Return (from inception through current date)								**11.8%**
DG Portfolio Annualized Return Goal (Mid-to-High Single Digit Returns)								7.5%
DG Portfolio Annualized Return Outperformance								**4.3%**

UR = Under Review

This portfolio is not a real money portfolio. Data as of February 1, 2017. Cost basis includes commissions. Results include divdends, but no interest received on cash balance.

DIVIDEND GROWTH PORTFOLIO -- as of February 1, 2017 — Fundamental data as of February 1, 2017

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	3.42%	mid Mar 2017	mid Mar 2017 (quart)	1.1	GOOD	GOOD	$58.00	6	1.23
Apple (AAPL)	2.28	1.77%	late Apr 2017	May 2017 (quart)	5.0	EXCELLENT	EXCELLENT	$159.00	7	0.81
Alerian MLP ETF (AMLP) New	0.96	7.28%	mid Feb 2017	late Feb 2017 (quart)	-	-	-	-	UR	-
Boeing (BA) New	5.68	3.46%	early May 2017	early June 2017 (quart)	1.8	GOOD	EXCELLENT	$159.00	5	1.03
Cisco (CSCO)	1.04	3.41%	early Apr 2017	Apr 2017 (quart)	3.0	EXCELLENT	EXCELLENT	$42.00	3	0.73
Coach (COH)	1.35	3.57%	early Mar 2017	early Mar 2017 (quart)	1.9	GOOD	GOOD	$41.00	6	0.92
Cracker Barrel (CBRL)	4.60	2.93%	mid Apr 2017	May 2017 (quart)	1.7	GOOD	GOOD	$171.00	6	0.92
CVS Health (CVS) New	2.00	2.57%	mid Apr 2017	Apr 2017 (quart)	1.0	GOOD	GOOD	$103.00	9	0.76
Energy Sector SPDR (XLE)	1.92	2.66%	late Mar 2017	early Mar 2017 (quart)	-	GOOD	NEUTRAL	-	UR	-
General Electric (GE)	0.96	3.23%	mid Mar 2017	Mar 2017 (quart)	3.1	EXCELLENT	GOOD	$36.00	6	0.82
General Motors (GM)	1.52	4.21%	early Mar 2017	Mar 2017 (quart)	2.0	GOOD	GOOD	$43.00	6	0.84
Hasbro (HAS)	2.04	2.48%	late Apr 2017	May 2017 (quart)	1.8	GOOD	EXCELLENT	$76.00	6	1.08
Hanesbrands (HBI) New	0.60	2.58%	late Apr 2017	late May 2017 (quart)	1.8	GOOD	EXCELLENT	$30.00	6	0.77
Intel (INTC)	1.04	2.85%	early Feb 2017	Feb 2017 (quart)	2.7	GOOD	GOOD	$42.00	7	0.87
Johnson & Johnson (JNJ)	3.20	2.83%	mid Feb 2017	Feb 2017 (quart)	2.7	GOOD	EXCELLENT	$121.00	7	0.94
Medtronic (MDT)	1.72	2.26%	late Mar 2017	Mar 2017 (quart)	1.6	GOOD	EXCELLENT	$76.00	4	1.00
Microsoft (MSFT)	1.56	2.45%	mid Feb 2017	Feb 2017 (quart)	2.5	GOOD	EXCELLENT	$56.00	7	1.14
Proctor & Gamble (PG)	2.68	3.07%	mid Apr 2017	early May 2017 (quart)	1.5	GOOD	EXCELLENT	$70.00	3	1.25
PP&L (PPL)	1.52	4.35%	late Mar 2017	late Mar 2017 (quart)	Held for diversification reasons.			$33.00	3	1.06
Realty Income (O)	2.53	4.34%	monthly	monthly	2.0	GOOD	GOOD	$59.00	3	0.99
S&P Dividend ETF SPDR (SDY)	2.13	2.49%	mid Mar 2017	late Mar 2017 (quart)	-	-	-	-	UR	-
Vanguard REIT ETF (VNQ)	2.96	3.64%	late Mar 2017	Mar 2017 (quart)	-	GOOD	NEUTRAL	-	UR	-

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

Exxon Mobil...from page 4

billion in 2016, as the ongoing rebalancing of the global crude oil markets makes exploration spending and other investments in the business increasingly more attractive. We'll be watching implications on traditional free cash flow measures, however, in the event energy resource pricing potentially turns for the worse.

Shares of Exxon are currently trading in the lower half of our fair value range, though we note the sizeable margin of safety we use in estimating the intrinsic value of the company. A look at free cash flow trends and capital spending initiatives through the course of the energy market cycle is quite telling of its free cash flow volatility. There's still a lot to like about the company's integrated upstream and downstream operations (and chemicals business), its fortress credit rating, and solid free cash flow generating capacity during times of economic duress, but we still prefer the XLE, which includes a sizable chunk of Exxon Mobil in it anyway. With the XLE, a devastating income-related event such as when ConocoPhillips and Kinder Morgan slashed their respective payouts just isn't a high probability.

Consumer Staples: Product Pricing Gains To Wane in 2017?

By Kris Rosemann

Valuentum President of Investment Research Brian Nelson's prediction for the prices of many consumer staples (XLP) stocks to underperform in 2017 continues to be based on valuation considerations and potentially shifting capital allocation preferences of investors, but we're adding a less-than-optimal product pricing environment to the list of factors that could potentially weigh on the sector in the year. Many consumer staples entities have become used to being able to raise product prices at will, regardless of the economic environment, but recent results have called into question whether consumers are still willing to pay more year after year for the same everyday products.

On January 27, Colgate-Palmolive (CL) reported a 4.5% drop in reported revenue in the fourth quarter of 2016 as global unit volumes fell 5.5% and foreign exchange headwinds of 1.5% overwhelmed product pricing gains of 2.5% in the period. Cost savings initiatives helped boost gross and operating margins in the quarter, but an increased emphasis on profitable volume growth rather than direct product pricing initiatives should now be expected to drive organic sales growth through the remainder of 2017--a statement that has caught our attention, even if lower commodity costs, a rather benign condition, is mostly to blame for the tactical change in pricing strategy.

> *From Colgate-Palmolive's conference call:* **The growth we deliver in 2017 is expected to rely on less pricing** with a sharpened focused on profitable volume growth for the full year starting in quarter one. And from an organic sales point of view we expect to see sequential improvement in quarter one.

Please see *Consumer Staples*...on next page

*Consumer Staples...*from previous page

On January 24, Kimberly-Clark (KMB) issued a similar warning about the lessening impact of product pricing gains in 2017 after its own cost savings program helped it to a fourth quarter-earnings beat. Developing and emerging markets helped drive a 1% gain in organic sales growth in the period as a 2% increase in volumes was partially offset by a combination of the negative impact of a product mix shift, net selling prices and foreign currency exchange rates compared to the fourth quarter of 2015. Kimberly-Clark is expecting only modest pricing gains, if any at all, during 2017:

> *From Kimberly-Clark's earnings press release*: Organic sales growth of approximately 2 percent, driven by higher volumes. Net selling prices and product mix expected to be similar, or **up slightly**, year-on-year.

Though we're not ready to say product pricing growth is no longer a key and defining characteristic of the consumer staples business model, if Colgate-Palmolive's and Kimberly-Clark's results are indicative of what is to come this year, investors might have to get used to the idea of product pricing growth not being the core area of top-line resilience for several consumer-staples entities in the near term, or at least not as strong of a contributor to the top line in the near term.

In light of this dynamic, the need to optimize costs to combat an intensifyingly-promotional retail environment in North America has become paramount. Opportunities to hike prices in emerging markets have also waned, too. Dividend Growth Newsletter portfolio holding Procter & Gamble (PG) increased its organic sales growth guidance for its fiscal 2017 (ends June 30) January 20, though it too has struggled to benefit from pricing gains that we have become used to seeing from consumer staples bellwethers. Consumers' wallets may be getting stretched.

> *From Procter & Gamble's earnings press release*: Organic sales increased two percent driven by a two percent increase in organic volume. **Pricing and mix had no net impact on sales** for the quarter.

It is growing increasingly likely that a perfect storm of disappointment may be lining up for some of the steadiest businesses in 2017, especially if volume growth comes up short. US-based multinational corporates are facing considerable uncertainty as President Trump continues to make his presence felt on American foreign policy. Border taxes, the dissolving of trade agreements, and immigration bans appear to be the start of the policy changes, but the end may be far from near.

Foreign exchange rates will remain volatile, and we continue to assess their impact on the sentiment of the global consumer and the reported results of US firms doing business overseas. Though commodity prices are expecting to provide some relief on the cost side in 2017 (arguably part of the reason why

Please see *Consumer Staples...*on next page

Consumer Staples...from previous page

product pricing gains are waning), emerging markets will likely need to see a sustained rebound in their economies before consumers there are willing and able to once again accept price hikes on the part of global consumer staples firms.

As with most consumer staples equities, the valuations of both Kimberly-Clark and Colgate-Palmolive are rather rich, further supporting our expectation for 2017 to be a difficult year for the sector. Shares of Kimberly-Clark, for example, are currently trading at ~19.2 times the midpoint of 2017 net-income-per-diluted-share guidance, while Colgate-Palmolive's shares are changing hands at more than 23.8 times management's guidance for 2017 GAAP earnings per share. Shares of both companies are trading firmly in the upper half of our respective fair value ranges.

Though their valuations may be stretched, we continue to be positive on the dividend health of both Colgate-Palmolive and Kimberly-Clark, even as we note the loss of a major product pricing lever could impact the pace of dividend expansion in the near term. Interestingly, we believe their respective dividend track records are a factor in the current over-inflated nature of their valuations (as stock buyers may be focusing more on the past than what lies ahead) as 2017 is expected to mark Kimberly-Clark's 45th consecutive year of an increase in the annual dividend, and Colgate-Palmolive has more than a half century of consecutive annual dividend increases under its belt. Shares currently yield ~3% and ~2.4%, respectively, and both firms' Dividend Cushion ratios are above 1 with generally good dividend safety ratings.

But as attractive as their respective dividend growth profiles may be, the potential for capital erosion is too great for us to gather serious interest in adding another one of these steady dividend payers to the Dividend Growth Newsletter portfolio in the near term. Unlike in the case where we recently added Boeing (BA) to gain exposure to industrials and the attractive aerospace industry specifically (areas lacking in the Dividend Growth Newsletter portfolio at the time), we're comfortable with our current exposure to the overheated consumer staples space in the Dividend Growth Newsletter portfolio via Procter & Gamble. We still want some exposure to these great business models, but we don't necessarily want to double-down on what could be a bad bet on the basis of valuations considerations. We'll be watching developments closely as we continue to weigh the risk-reward profile of consumer staples equities through the course of 2017 and beyond.

Novartis' Continuous Dividend Growth and Promising Pipeline

By Alexander J. Poulos and Brian Nelson, CFA

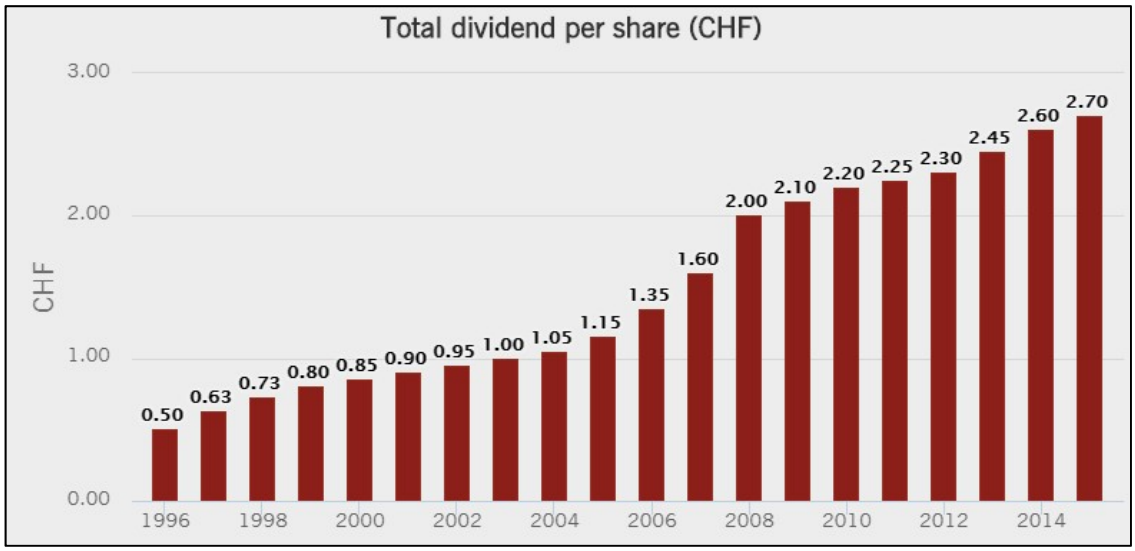


Image Shown: Novartis' dividend history, source: Novartis.

Please see *Novartis' Continuous*...on next page

*Novartis' Continuous...*from previous page

Sometimes the most attractive opportunities manifest themselves in companies that are in the midst of a transition. In the case of entities in the pharmaceutical industry, the transition often occurs during the period of patent-protection loss of a top-selling treatment. Typically, the market will sour on the company's prospects as revenue is expected to decline in the near term. However, the longer investment time horizon we have at Valuentum allows us to examine whether such opportunities still fit for inclusion in the newsletter portfolios. Said differently, we're less interested in what the company will do in the next quarter or two than we are in the company's competitive advantages and its discounted cash-flow derived intrinsic worth. If the long-term is still bright, we can overlook temporary near-term challenges.

Overview

Novartis (NVS) is a well-diversified pharmaceutical powerhouse based in Switzerland. The company is far from a household name in the US, but to draw a fair comparison based on market capitalization, a close competitor is Pfizer (PFE) at nearly $200 billion (we're talking about mega-cap). The comparison with Pfizer gains increasing relevance, too, as Novartis like Pfizer does not exclusively rely on patent-protected pharmaceuticals to derive the bulk of its revenue stream. The diversity of Novartis' revenue stream allows for a generous return of capital to shareholders in the form of an increasing annual dividend, a noted difference from the quarterly payout of Pfizer, which was cut when the latter bought Wyeth a number of years ago. The analysis below details the three most important divisions of Novartis beginning with its Pharmaceuticals division.

Pharmaceuticals

The Pharmaceutical segment remains the most dynamic area of Novartis. The company remains on pace to bring forth three novel products that together we estimate will more than offset the revenue loss from key products. Novartis recently lost patent protection of its top-selling product Gleevec after a long and fruitful run. The move was not unexpected; the groundwork has been put in place to offset the loss, but Novartis is now firmly in the penalty box as revenue is expected to drop when the company reports 2016 numbers.

To streamline its product portfolio and to concentrate on areas of noted strength, Novartis had entered into a deal with fellow European pharma heavyweight GlaxoSmithKline (GSK) in 2014 to purchase Glaxo's Oncology division while combining their respective consumer health groups. Novartis exited the vaccine market by divesting the bulk of its line to Glaxo as well. Novartis gained a host of novel oncology properties expanding its formidable presence in oncology. Thus far, oncology therapies have remained resistant to hardball negotiating tactics by the PBM's, and while there are no guarantees that payers will not balk over price, oncology remains the premier area of focus for the pharma/biotech sector. Novartis internal R&D efforts have begun to bear fruit with three important compounds on pace to exceed the revenue lost from the expiration of Gleevec's patent ($4.74 billion in sales for 2015).

The first compound worthy of discussion is Cosentyx, Novartis entrance into the crowded field of inflammatory diseases. Cosentyx is an interleukin 17-a antagonist, for the treatment of a host of inflammatory diseases, most notably psoriasis. The treatment requires subcutaneous injections similar to other treatments such as Humira and Enbrel. Treatment of inflammatory disease with a biological agent such as Cosentyx comprises the largest treatment cohort of specialty pharma. The rapid growth of specialty pharma is approaching par with traditional oral dosage forms. In the current environment where PBM's are looking to get a handle on the rising cost of therapies, the biological treatments for inflammatory disease offer a particularly enticing target for hardball negotiating tactics.

Evidence of the PBM's taking a harder stance has recently been exposed from Amgen (AMGN) where the company doesn't expect to be able to raise prices on Enbrel in 2017 (as disclosed in the most recent conference call). We raise the specter of increasing cost scrutiny to offer a more balanced view of the opportunity in Cosentyx, even as we say that Cosentyx remains well on pace to post sales in 2016 in excess of $1 billion dollars, cementing the treatment as a blockbuster product.

Please see *Novartis' Continuous...*on page 13

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

By Valuentum Analysts

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

Though our dividend-growth portfolio 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 Yiel	VBI	Div Growth	Div Cushion
AbbVie	ABBV	Health Care	4.2%	7	GOOD	1.1
Digital Realty Trust	DLR	Financials	3.7%	7	GOOD	1.7
Darden Restaurants	DRI	Consumer Discretionary	3.6%	7	GOOD	1.3
IBM	IBM	Information Technology	3.3%	7	EXCELLENT	1.4
Intel	INTC	Information Technology	2.9%	7	GOOD	2.7
Williams-Sonoma	WSM	Consumer Discretionary	2.7%	7	EXCELLENT	2.6
Johnson & Johnson	JNJ	Consumer Staples	2.7%	7	EXCELLENT	2.7
Microsoft	MSFT	Information Technology	2.5%	7	EXCELLENT	2.5
United Technologies	UTX	Industrials	2.4%	7	EXCELLENT	1.4
Raytheon	RTN	Industrials	2.1%	7	EXCELLENT	2.2
CVS Caremark	CVS	Consumer Staples	2.1%	9	GOOD	1.0
Apple	AAPL	Information Technology	1.9%	7	EXCELLENT	5.0
Manpower	MAN	Information Technology	1.9%	7	EXCELLENT	3.4
Ralph Lauren	RL	Consumer Discretionary	1.8%	7	EXCELLENT	3.5
Deluxe	DLX	Information Technology	1.6%	7	GOOD	4.6
Canadian National	CNI	Industrials	1.6%	7	EXCELLENT	1.7
Oracle	ORCL	Information Technology	1.5%	7	EXCELLENT	4.8
Jabil Circuit	JBL	Information Technology	1.5%	9	GOOD	3.3
Ashland	ASH	Materials	1.3%	7	GOOD	2.9
H.B. Fuller	FUL	Materials	1.2%	7	EXCELLENT	2.3
FedEx	FDX	Industrials	0.8%	7	GOOD	1.1
Visa	V	Information Technology	0.7%	7	GOOD	5.6
Dillard's	DDS	Consumer Discretionary	0.4%	7	GOOD	12.3

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

The Financially-Healthiest Dividend Payers Yielding Over 2%

By Valuentum Analysts

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

Enter stocks that have the highest multiplicative combination of their dividend yield and Dividend Cushion ratio. We exclude the business models of master limited partnerships and real estate investment trusts in this screen and focus exclusively on corporates. Income investors have a lot to choose from, and this screen is one of our favorites -- it focuses on identifying the financially-healthiest dividend-payers with yields over 2%. We've overlayed the screen with an Economic Castle assessment to consider business-model risk, too!

Company Name	Symbol	Est. Div Yiel	Div Cushion	Economic Castl	Multiplie
Automatic Data Processing	ADP	2.2%	7.5	Very Attractive	16.65
GameStop	GME	5.7%	2.4	Very Attractive	13.85
Guess	GES	7.2%	1.7	Attractive	12.11
Abercrombie & Fitch	ANF	6.7%	1.8	Unattractive	12.02
Computer Prog and Syst	CPSI	5.5%	2.0	Very Attractive	10.99
AVX Corp	AVX	3.0%	3.6	Attractive	10.86
Cisco	CSCO	3.5%	3.0	Very Attractive	10.35
QUALCOMM	QCOM	3.9%	2.6	Highest Rated	10.22
Resources Connection	RECN	3.1%	3.3	Very Attractive	10.08
American Eagle	AEO	3.3%	2.9	Attractive	9.74
General Motors	GM	4.7%	2.0	Attractive	9.48
General Electric	GE	3.1%	3.1	Attractive	9.44
CA Tech	CA	3.2%	2.9	Highest Rated	9.29
Finish Line	FINL	2.1%	4.1	Attractive	8.78
Hewlett-Packard	HPQ	3.6%	2.4	Unattractive	8.78
Best Buy	BBY	2.4%	3.5	Attractive	8.37
Chico's FAS	CHS	2.3%	3.6	Attractive	8.23
Gap	GPS	3.8%	2.1	Attractive	7.98
Garmin	GRMN	4.3%	1.8	Attractive	7.91
Intel	INTC	2.9%	2.7	Attractive	7.80
Paychex	PAYX	3.0%	2.6	Very Attractive	7.65
Pfizer	PFE	3.5%	2.2	Attractive	7.63
CoreCivic	CXW	7.1%	1.1	Attractive	7.53
Taiwan Semiconductor	TSM	3.2%	2.3	Attractive	7.53
Intersil	ISIL	2.2%	3.4	Highest Rated	7.33
Superior	SUP	2.6%	2.8	Attractive	7.25
Johnson & Johnson	JNJ	2.7%	2.7	Attractive	7.22
World Wrestling	WWE	2.6%	2.7	Very Attractive	7.22
Williams-Sonoma	WSM	2.7%	2.6	Attractive	7.16
Cypress Semi	CY	4.0%	1.8	Attractive	7.15
Cardinal Health	CAH	2.4%	2.9	Very Attractive	7.12
Archer-Daniels-Midland	ADM	2.9%	2.5	Attractive	7.06
Xilinx	XLNX	2.4%	3.0	Very Attractive	7.06
Coach	COH	3.6%	1.9	Attractive	6.87
Western Union	WU	2.8%	2.4	Neutral	6.85
Sysco	SYY	2.3%	2.8	Attractive	6.57
Abbott	ABT	2.5%	2.7	Attractive	6.56
Nu Skin	NUS	2.2%	3.0	Attractive	6.53
Emerson Electric	EMR	3.7%	1.8	Attractive	6.51
NTT Docomo	DCM	2.0%	3.2	Attractive	6.50
Accenture	ACN	2.1%	3.1	Very Attractive	6.43
Boeing	BA	3.6%	1.8	Attractive	6.37
Microsoft	MSFT	2.5%	2.5	Very Attractive	6.33
H&R Block	HRB	3.9%	1.6	Very Attractive	6.31
Celenese	CE	2.2%	2.8	Attractive	6.31
Interpublic	IPG	2.5%	2.4	Very Attractive	6.15
Target	TGT	3.4%	1.8	Attractive	6.11
STMicroelectronics	STM	2.2%	2.7	Attractive	6.10
Bristol-Myers Squibb	BMY	3.2%	1.9	Very Attractive	6.05
Acuity Brands	AYI	0.3%	23.7	Attractive	6.04

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 Yiel	Div Safety	Div Cushion
Textainer	TGH	Rental and Leasing	1.2%	VERY POOR	-80.8
CONSOL Energy	CNX	Industrial Minerals	0.2%	VERY POOR	-65.1
KB Home	KBH	Homebuilders	0.7%	VERY POOR	-38.9
Windstream	WIN	Telecom Services - diversified	6.7%	VERY POOR	-36.1
Alcoa	AA	Aluminum	0.4%	VERY POOR	-33.6
Lennar	LEN	Homebuilders	0.3%	VERY POOR	-25.6
Devon Energy	DVN	Independent Oil & Gas	0.5%	VERY POOR	-18.5
Anadarko	APC	Independent Oil & Gas	0.3%	VERY POOR	-13.5
Ryder System	R	Rental and Leasing	2.3%	VERY POOR	-8.0
Tailored Brands	TLRD	Retail - Men's, Women's, Kids' Apparel	3.2%	VERY POOR	-6.7
Allegheny Technologies	ATI	Aluminum	1.8%	VERY POOR	-5.4
D. R. Horton	DHI	Homebuilders	1.0%	VERY POOR	-5.3
Barrick Gold	ABX	Metals & Mining - gold	0.5%	VERY POOR	-4.8
Koppers	KOP	Building Materials	3.1%	VERY POOR	-4.5
MDC	MDC	Homebuilders	4.0%	VERY POOR	-4.4
Yamana Gold	AUY	Metals & Mining - gold	0.7%	VERY POOR	-4.3
Rent-A-Center	RCII	Rental and Leasing	2.7%	VERY POOR	-3.4
Ball Corp	BLL	Containers & Packaging	0.7%	VERY POOR	-3.1
Hill-Rom	HRC	Medical Instruments	1.1%	VERY POOR	-2.8
Olin Corp	OLN	Chemicals - mid/small	3.9%	VERY POOR	-2.7
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
Murphy Oil	MUR	Refiners	3.2%	VERY POOR	-2.2
Noble Energy	NBL	Independent Oil & Gas	1.0%	VERY POOR	-2.2
Huntsman	HUN	Chemicals - broad	2.8%	VERY POOR	-2.0
Quad/Graphics Inc	QUAD	Book Publishing	4.8%	VERY POOR	-2.0
Service Corp Intl	SCI	Personal Services	2.0%	VERY POOR	-1.9
Apache	APA	Independent Oil & Gas	1.5%	VERY POOR	-1.7
Hess	HES	Refiners	1.6%	VERY POOR	-1.7
Centurylink	CTL	Telecom Services - diversified	7.8%	VERY POOR	-1.7

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

*Novartis' Continuous...*from page 9

In clinical trials, Cosentyx registered superior outcomes compared to Enbrel and Johnson and Johnson's (JNJ) Stelara. The head to head data is key; this allows the product to differentiate itself in the eyes of the payers. The PBM's will look to cover the most effective product, and with Cosentyx posting superior outcomes, the product might be able to take meaningful share from Stelara. To add additional context as to the upside of the product, Stelara posted sales of $2.3 billion in the first three quarters of 2016.

Novartis is conducting an outcomes trial comparing Cosentyx to top selling product Humira. A positive head-to-head result will further support Cosentyx as the optimal choice in the treatment of psoriasis. If Cosentyx is able to post superior results in this trial, a credible case could be made that Cosentyx by itself will replace the revenue lost from Gleevec. We'll continue to monitor developments.

Slides

Inflammatory Disease Remains a Key Driver of the Specialty Drug Trend

			Trend		
Rank	Therapy Class	PMPY Spend ($)	Utilization (%)	Unit Cost (%)	Total (%)
1	Inflammatory conditions	89.10	10.3	14.7	25.0
2	Multiple sclerosis	53.31	3.5	6.2	9.7
3	Oncology	49.62	9.3	14.4	23.7
4	Hepatitis C	38.44	-2.2	9.2	7.0
5	Human immunodeficiency virus	31.53	4.6	12.0	16.6
6	Growth deficiency	7.12	2.8	2.8	5.6
7	Cystic fibrosis	6.64	12.5	40.9	53.4
8	Pulmonary hypertension	5.85	13.4	4.8	18.1
9	Hemophilia	5.79	4.9	15.4	20.4
10	Sleep disorders	4.57	5.5	18.5	24.1
	Total Specialty	$341.21	6.8%	11.0%	17.8%

Express Scripts. Drug Trend Report 2015. Available at: http://lab.express-scripts.com/lab/drug-trend-report. Accessed April 11, 2016.

Image Source: Express Scripts

Entresto

Entresto is a novel new treatment for heart failure. The compound is a combination of Sacubitril a Neprilysin Inhibitor and Novartis' recent blockbuster Diovan (Valsartan). Thus far, the utilization of the product is not up to the initial hopes of management as the payers required a prior authorization before paying for the product.

The lack of favorable formulary placement is a major impediment to sales growth in 2016, with net sales of $200 million in the US expected for 2016. Management remains confident it will be able to rectify the formulary issue with an aggressive push to negate the need for a prior authorization. Aiding in this endeavor is recent data that indicates the product is efficacious.

Please see *Novartis' Continuous...*on next page

*Novartis' Continuous...*from previous page

Though we remain in a "show me state," the data is indeed compelling. We continue to monitor the weekly IMS Rx data to determine if Entresto remains on the right path, but thus far, the number of prescriptions filled continues to point north. We're encouraged.

As a novel new agent with a large addressable market, Entresto is a particularly noteworthy compound. The key for Novartis, however, will be to unlock the PBM's initial resistance towards covering the product. Due to the lack of meaningful competition, Entresto has the potential to become one of Novartis top-selling products.

Ribociclib

Novartis' Oncology division is a source of future innovation with a promising new therapy for breast cancer. Ribociclib is a new treatment that was recently granted breakthrough therapy designation by the FDA. Ribociclib is designed to be used in conjunction with letrozole to treat women with postmenopausal HR+/HER2- advanced or metastatic breast cancer. The combo would be a first line treatment, a key designation as it should allow for maximum uptake.

Thus far in individual trials, Ribociclib has shown to be slightly more efficacious than category leader Pfizer (PFE) Ibrance. Novartis is conducting a head to head study; a positive outcome would allow Ribociclib to vault past Ibrance, becoming the top-selling product in its class. Thus far, the oncology properties have proven to be remarkably resistant to pricing pressure from the individual payers--a win here would set up a lucrative annuity-like revenue stream for Novartis.

In November, the FDA issued a priority review for Ribociclib, which will shorten by ten months the decision process. A PDUFA date for Ribociclib has not been assigned at the time or is in writing; we expect a decision within six months of the FDA acceptance of the application, which is dated November 1, 2016, at some point before the end of the second quarter

Siponimod

In a strategic bit of lifecycle management, Novartis' Multiple Sclerosis franchise faces the loss of patent exclusivity of its top-selling product Gilenya. The patent is expected to expire in 2019. Gilenya accounted for $2.7 billion in sales in 2015 and continued to ramp higher.

Novartis, however, scored an impressive clinical win with stunning results for Siponimod for the treatment of secondary progression multiple sclerosis. The key for Novartis is the category remains an area of significant unmet need, which should allow the company to ramp sales at an aggressive rate. Siponimod is competing in a wide open field versus Gilenya which needs to contend with multiple existing products such as Teva's (TEVA) Copaxone and Biogen's (BIIB) Tecfidera. Novartis has a clear path to establishing Siponimod as the primary standard of care for the indication of secondary progressive multiple sclerosis which should go a long way towards recouping the expected loss of Gilenya revenue in 2019. Assuming, Siponimod continues its impressive streak of results, a credible case could be made that the product might eclipse the sales of Gilenya.

Novartis continues its research-based focus with numerous compounds in various stages of the investigation. The list above highlights some of the most promising near-term candidates. The field remains uncertain with many surprises both positive and negative that can manifest themselves at any time. One example in particular was Siponimod, which was not even identified as one of Novartis top molecules--it came out of the blue in a positive manner. The second division worth examination is the Sandoz division that manufactures generic equivalents and biosimilars, an area of particular focus.

Sandoz

The Sandoz Division manufactures pharmaceutical products that have lost patent exclusivity. The field is notoriously competitive with little in the way to distinguish operations from competitors. Sandoz, however, does offer Novartis an attractive opportunity to manage the patent loss of some of its principal

Please see *Novartis' Continuous...*on next page

*Novartis' Continuous...*from previous page

products. If Sandoz is the first to file for an authorized generic of a product, the division will be granted a six-month exclusive window to manufacture the only authorized generic of the product.

Once the six-month exclusivity lapses, however, the margins plummet as additional competitors enter the market. Once the six-month exclusive window lapses, the product will behave in a similar manner as a commodity, rising and falling based on the number of competitors in the market. Typically, however, the price will collapse and stay depressed. For Novartis, we like that the company can maintain the bulk of the branded sales (just a bit longer) by transferring the branded product to their Sandoz division, making the exercise worthwhile.

The Sandoz division accounted for ~20% of Novartis' overall sales in 2015, but accounted for only ~10% of operating income due to the lower margins that come with making generic medications. The key driver going forward is Sandoz's burgeoning biosimilar division, which is on pace to produce equivalents of many of the top-selling biologic agents. Thus far, Sandoz has authorized biosimilars of Copaxone 20mg and Neupogen, in addition to unanimous approval for a bioequivalent of Enbrel. Sandoz did suffer a notable setback in the quest for a biosimilar for Neulasta by receiving a complete response from the FDA. Sandoz will need to address the deficiencies noted and refile, delaying the process.

The Sandoz Division offers Novartis a clear path to profit from the burgeoning field of biosimilar equivalents of top-selling products. The biotech field is rapidly evolving, and the rise of biosimilars has shaken the industry; it is no longer feasible to rest on the laurels of decades-old innovations. These compounds will now face the same price competition as solid dosage forms. The older more established companies who have not meaningfully diversified their product line are at particular risk as multiple companies are vying for a piece of their once formidable sales.

The payers of the world, most notably governments, are keen to keep price competition heated in an attempt to corral price, as the demographic tidal wave descends on each countries' healthcare budget. Great rewards await the companies that can bring forth novel new treatments to address the various ills plaguing humankind.

Alcon

The final division worth noting is the troubled Alcon eye care division. Novartis acquired Alcon in a series of purchases with the final price tag eclipsing $50 billion dollars. Thus far, the move has been a disappointment with hoped-for deal synergies failing to materialize. Alcon's key product Lucentis continues to lose market share as Regeneron's (REGN) Eyelea continues to take share. Further complicating matters is the weak sales in its surgical division with plans in place to turn around the division.

The market remains rife with rumors that Novartis may seek to divest Alcon to pursue other fast-growing fields. We do not share the view, as Novartis' debt load leaves it sufficient firepower to make tuck-in acquisitions, as needed. Thus far, the management team has indicated an appetite for smaller complementary deals instead of larger more expensive deals. We continue to share the cautious stance of management, as market caps remain elevated in the mid-to-late stage biotech companies.

To Novartis credit, it made a couple of tuck-in acquisitions at the end of 2016, acquiring Encore Vision to bolster the offerings of the Alcon division. Also, right at the end of the year, Novartis paid $50 million to gain an option on Conatus Pharmaceuticals NASH candidate. It remains to be seen if either product will bear fruit, but we like the low-cost approach in these efforts. Novartis is gaining access to some innovative products at a modest cost.

Dividend*

As a diversified company in a number aspects of the drug delivery universe, Novartis generates a substantial amount of free cash flow. During the past three years, for example, cash flow from operations has hovered between $12-$14 billion, while capital spending has been between $2-$3 billion, good for

Please see *Novartis' Continuous...*on next page

*Novartis' Continuous...*from previous page

about $10 billion in run-rate free cash flow generation capacity (it allocated $6.6 billion to the dividend in 2015).

The primary method employed to return cash to shareholders remains the annual dividend. As is typical of European equities, the dividend is distributed once a year, unlike the quarterly payouts that dominate the US market. We rate Novartis' Economic Castle as attractive, and we do not believe the company will have any difficulty raising the dividend in coming years. At this time we are not prepared to add Novartis to the Dividend Growth Newsletter portfolio, but Novartis does have a collection of exciting branded products. We wanted to get this one in front of you in case we decide to pull the trigger on the idea.

** The price of Novartis' ADRs and the US dollar value of any dividends may be negatively affected by fluctuations in the US dollar/Swiss franc exchange rate.*

Disclosures: Alexander J. Poulos was long Novartis at the time of original publishing.

AT&T's Love Affair with Debt

By Brian Nelson, CFA

On January 25, AT&T (T) wrapped up 2016 with a rather solid fourth-quarter report, and full-year results weren't bad. We have no qualms with AT&T, but as with Verizon (VZ), we worry the company has stretched its balance sheet too far this late into the economic cycle.

Contributions from AT&T's acquisition of DIRECTV and gains in IP services and video helped drive consolidated revenues 11.6% higher during 2016, while adjusted operating income came in at $31.8 billion versus $27.7 billion in the prior year. Importantly, AT&T's full-year cash flow from operations was a record $39.3 billion, up from $35.9 billion in 2015, while capital expenditures, including capitalized interest, came in at $22.4 billion, versus $20 billion in 2015, translating to free cash flow generation of $16.9 billion in 2016, up a cool billion from 2015. AT&T's free cash flow dividend payout ratio for the full year was a comfortable 70%, and we like companies that continue to generate free cash flow far in excess of cash dividends paid.

AT&T looks to continue to build on the transformational year that was 2016, and we're encouraged by its 5G evolution plans and improved spectrum position, even as industry pricing competition from the likes of Sprint (S) and T-Mobil (TMUS) remains intense. The company's deal to acquire Time Warner (TWX) for a total transaction value of more than $100 billion, announced in October, looks like it will shake up the industry. HBO and CNN, prized assets at Time Warner, would serve to complement AT&T's distribution network nicely, and Time Warner's film/TV studio and unrivaled library of entertainment is simply hard not to like. In light of management's demonstrated ability to deliver on the $1.5 billion in DIRECTV cost synergies, we're also optimistic about what the potential Time Warner transaction may bring to margin improvement (operating income margin was 19.4% in 2016 versus 18.8% in 2015). The regulatory road may still have obstacles to overcome, however, as President Trump seems to privately oppose the deal; after all, how can we forget his claims that CNN is "fake news:"

Please see *AT&T's Love Affair...*on next page

***AT&T's Love Affair...*from previous page**

As we watch steps toward deal completion, AT&T's financial outlook for 2017, excluding any impact from the pending Time Warner tie-up, is pretty good. AT&T expects consolidated revenue growth in the low-single-digits, adjusted earnings per share growth in the mid-single-digits, and ongoing adjusted operating margin expansion. Capital spending will be roughly at 2016 levels, and free cash flow is targeted to advance to the $18 billion range, implying ongoing improvement over last year's levels. In the twelve months ending December 2016, the company paid out $11.8 billion in cash dividends, so free cash flow coverage of the dividend will remain robust. AT&T is doing a lot of things right.

That said, what keeps us up at night is the incremental debt that will be needed to finance the pending Time Warner transaction. Though AT&T expects its net debt to adjusted EBITDA to be in the 2.5 times range at the end of the first year after closing, adding ~$40 billion to its existing balance sheet (it took out a $40 billion bridge loan related to the deal) brings its total net debt load north of $157 billion, a number that includes debt maturing within one year. Corporate America's love affair with debt-funded deal-making could come home to roost in a big way at AT&T, much to the detriment of income investors. AT&T's negative Dividend Cushion ratio considers its massive financial liabilities as an impediment to the pace of future dividend growth.

Boeing's Lift Off, Lockheed's Caution, and United Tech's Outlook

By Brian Nelson, CFA

In August 2016, we wrote an extensive update on the commercial aerospace market, and we encourage those that are digging into this follow-up note to read that piece first before proceeding. In this note, dated Wednesday, January 25, we'd like to build on that piece and update investors on a few insights we've gathered within the aerospace market.

First, what was once a key company to assess commercial aerospace demand is no longer. As of November 1, Alcoa (AA) has been severed into two independent publicly-traded entities, and its new split-off Arconic (ARNC), headed by industry giant Chairman and CEO Klaus Kleinfeld, is now the entity whose performance we expect to offer incremental insight into commercial airplane build rates and overall end market demand. Legacy Alcoa, which reported its first quarter as a separate company January 25, no longer represents an effective lead indicator to assessing end market demand across a variety of industries verticals, in our view. Times have changed, and that role has shifted to Arconic.

According to Arconic's Investor Day slides from December 2016, it is estimated that roughly 65% of the new company's business comes from the aerospace and transportation markets, including 22% from commercial airframes and 15% from commercial aero engines. Defense aerospace comes in at 4%. As Arconic puts it, "if it flies, we're on it," and the company has content on every Boeing (BA) platform, it has GRB sheets and plates on every Airbus (EADSY) platform, is a prominent supplier to Embraer (ERJ), and has exposure to the Joint Strike Fighter (JSF). We'll be looking for incremental insights when Arconic reports fourth-quarter 2016 results January 31, 2017.

Very few other industries have greater visibility that the commercial aerospace industry, not to be confused with the commercial airline industry, the latter comprising those that fly passengers from one place to another. Those that are involved in building planes continue to benefit from the burgeoning backlogs (order books) of the commercial airframe makers. In Boeing's fourth-quarter earnings report, released January 25, the aerospace giant noted that backlog remains robust at $473 billion with more than 5,700 commercial airplane orders. To put this size in perspective, Boeing delivered 748 commercial planes in 2016, 762 commercial planes in 2015, and the company expects to deliver between 760-765 commercial planes in 2017. Translation: Boeing has more than 7 years' worth of annual run-rate production just sitting in backlog!

We're huge fans of Boeing, of course, and while the company has considerable flexibility with program accounting to achieve bottom-line targets, we like expectations for GAAP earnings to come in the

Please see *Boeing's Lift Off...*on next page

***Boeing's Lift Off...*from previous page**

range of $10.25-$10.45 per share for 2017, putting the company at roughly 16 times current-year earnings at the prevailing market price at the time of this writing. Earnings are backed by strong cash flow from operations generation, too, with the aerospace giant targeting the measure to increase to ~$10.75 billion, slightly better than the mark achieved in 2016. Capital expenditures are expected to decline $300 million in 2017 from the previous year's levels, to $2.3 billion, so free cash flow should advance this year. Free cash flow came in at $7.9 billion during 2016, up from $6.9 billion in 2015. While many are worried about the contents of President Trump's next tweet, Boeing's core commercial business is knocking the cover off the ball.

Whereas Boeing boasts a massive commercial backlog in the hundreds of billions, suggesting increased visibility, Lockheed Martin's (LMT) entire backlog, on the other hand, stood at ~$96 billion, just shy of 2 times run-rate annual sales. That's still a huge order book, of course, and we can't be too upset with the company's strong performance in 2016---net sales: $47.2 billion in 2016, $40.5 billion in 2015, and earnings from continuing operations: $3.8 billion in 2016, $3.1 billion in 2015—but Lockheed's outlook for 2017 was quite cautious and probably for good reason. Trump's ongoing criticism of the costs of the F-35 program seems to have management preoccupied, and buried in the Lockheed's fourth-quarter press release was language stating that the company "expects to report a material weakness in internal control over financial reporting at its Sikorsky Aircraft Corporation business in its Annual Report."

Though the notification is probably nothing to worry about, we didn't like the news, and it seems likely Lockheed will probably make some tweaks to its top and bottom-line targets for 2017 as the year progresses. Right now, net sales and diluted earnings per share are targeted in the range of $49.4-$50.6 billion and $12.25-$12.55 per share respectively, implying that Lockheed's shares are trading at a lofty 20 times current-year earnings. On a relative value basis, we think Boeing offers a much better big-cap idea than Lockheed, and Boeing's ties to both the commercial and defense aspects of plane-making offer considerable diversification benefits to handle both the economic and political cycle. Further, we think Trump can impact the fate of Boeing much less than that of Lockheed Martin, given the latter's heavy defense exposure.

United Technologies' fourth-quarter report, released January 25, showed sales increasing 2% (all organic) and adjusted earnings per share advancing 5% for the full-year. The company affirmed its adjusted earnings per share target for 2017 in the range of $6.30-$6.60 on sales of $57.5-$59 billion, the former implying shares are trading at ~17 times current-year earnings at the high end of the guidance range at prevailing market prices at the time of this writing. We like United Technologies for its cash-flow conversion prowess, meaning that cash flow from operations of $6.4 billion during 2016 was nearly 30% higher than net income for the year, and 2016 free cash flow of $4.7 billion was an impressive 93% of net income. What this means is that United Tech's earnings are largely cash earnings and of high quality. As with Lockheed, United Tech's Pratt & Whitney engine division is focused on reducing costs on the F-35, and we'll be monitoring that program closely in the months ahead.

All in, commercial aerospace still looks fantastic, perhaps punctuated by Boeing's strong 2017 delivery outlook and its burgeoning aerospace backlog. Our favorite aerospace supplier had been Precision Castparts, but Warren Buffett scooped up that engine-casting supplier some time ago, and it is now within the Oracle's portfolio at Berkshire Hathaway (BRK.A, BRK.B). We include Berkshire Hathaway's B shares in the Best Ideas Newsletter portfolio largely for this reason (as our "play" on aerospace), but Boeing is looking more and more attractive as a dividend growth idea, too. Recently, Boeing raised its dividend 30%+ to an annual payout of $5.68 per share, implying a forward yield of ~3.4% at present prices. Shares of the aerospace giant have been rocketing higher.

Adding an Undervalued, Dividend Growth Prospect

By Kris Rosemann

The Dividend Growth Newsletter portfolio is sitting at 30%+ cash as of the release of the January edition, and we're expecting 2017 to be another good year for equity prices in general. As a result, we're actively looking for uses for the dry powder, and that's where Hanesbrands (HBI) comes in.

Hanesbrands is the largest basic apparel company in the world and has a history that stretches back more than a century. Its brand strength is undeniable with a lineup that includes Hanes, Champion, Playtex, and Bali, to name a few, and it boasts leading market-share positions in key categories around the world. Along with such a portfolio of brands comes pricing power, which helps the company combat potentially volatile input costs such as cotton. We're expecting Hanesbrands' pricing power to help it continue growing its top-line at a mid- to high-single digit rate in coming years, while the underwear giant has an annual target of double-digit earnings per share growth.

Hanesbrands looks compelling from a valuation point of view. Our fair value estimate for shares currently sits at $30, and its stock is changing hands at ~12 times expected fiscal 2016 earnings from continuing operations as of this writing. Due to such an attractive valuation profile, we've had our eyes on the company for some time. However, after it hiked its quarterly dividend January 24 to $0.15 from $0.11 (a 36%+ jump), we now feel the time is right to establish a 3% position in the Dividend Growth Newsletter portfolio (as the increase pushes the firm's dividend yield to ~2.5% from previous levels below 2%). After the large dividend hike, Hanesbrands' Dividend Cushion ratio is still a healthy 1.8, and it brings its dividend payout ratio to ~30% on expected 2016 numbers (based on the high end of management's adjusted earnings per share guidance), which is roughly in line with management's target payout ratio of 25%-30%. Looking into 2017 and beyond, we're expecting healthy bottom-line growth to translate into meaningful income generation for shareholders.

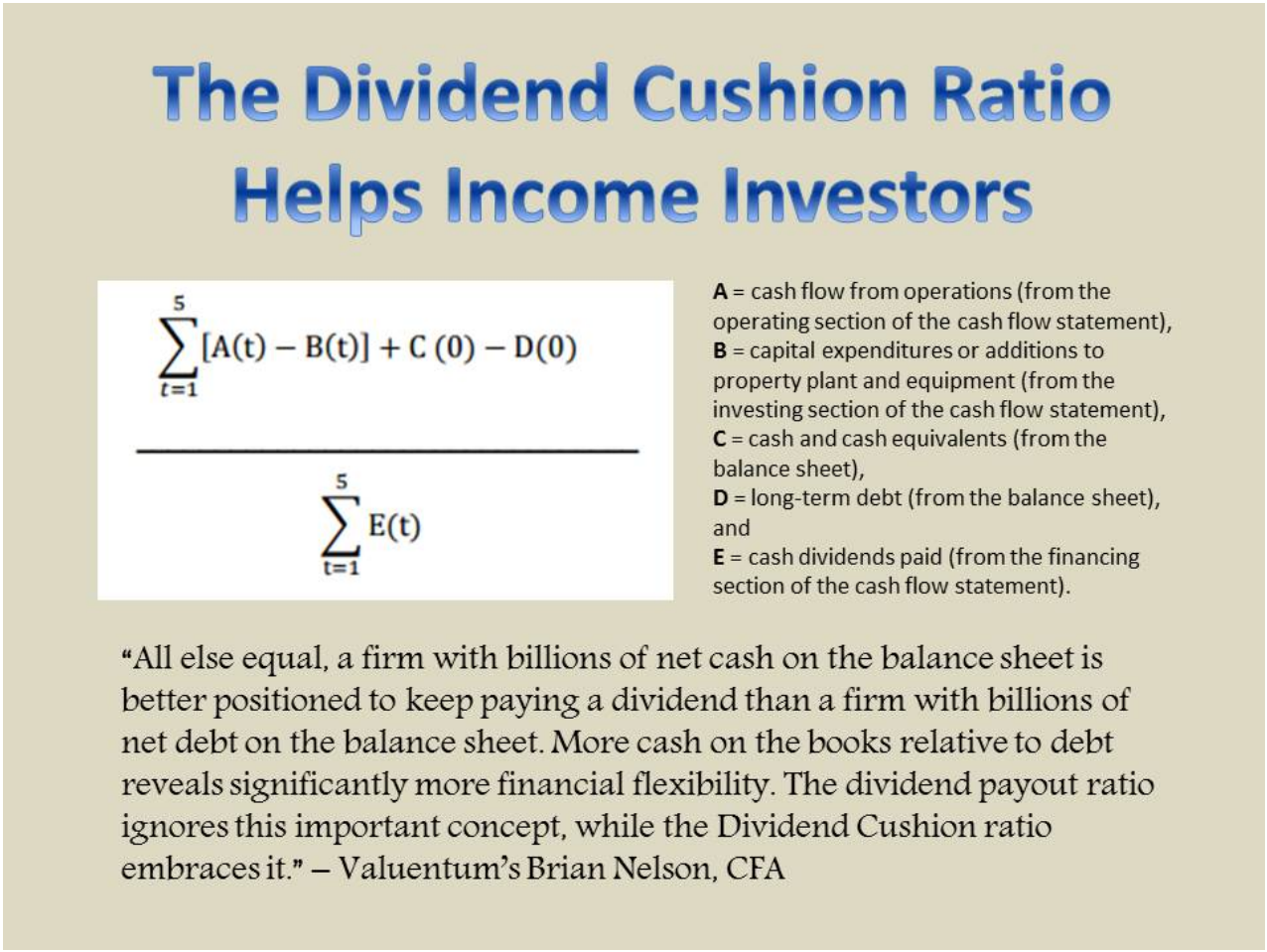
Though we like Hanesbrands' investment opportunity a lot, let's cover a couple risks to its dividend growth potential. As of the third quarter of 2016, the company's net debt load was more than $3.4 billion, which translates to a net debt-to-annualized EBITDA ratio of ~3.2 times on the basis of our estimates (management is targeting adjusted operating income of $955 million at the high end of its provided guidance range and a good estimate for D&A is ~$100 million for the year). In the future, management is planning to reduce net debt-to-EBITDA to the range of 2 to 3 times, meaning it will have to allocate a portion of its free cash flow to deleveraging in coming years. Though we prefer a net cash position on most of our dividend growth ideas, we think management is aware of the risks that come with leverage, and we hope to see progress toward debt reduction in coming periods.

Let's cover free cash flow. Free cash flow generation came in below cash dividends paid during fiscal 2015 (due to a sizable inventory build), but sales initiatives and inventory reduction efforts have been bearing fruit as of late, and we expect a return to previous years' free cash flow performance (and even better!). Cash flow from operations during fiscal 2014 and fiscal 2013 came in at ~$508 million and ~$591 million, while capital spending was ~$64 million and ~$44 million for those years, respectively, good for average free cash flow generation of ~$500 million during 2013-2014. Hanesbrands' updated 2016 guidance calls for record net cash flow from operations performance in the range of $750-$800 million on capital spending of ~$90 million, translating into expectations of free cash flow generation in the range of $660-$710 million for fiscal 2016. We estimate run-rate annual cash dividends paid after the hike to be ~$220 million revealing material coverage by free cash flow, to the tune of over 3 times.

In light of its valuation opportunity and improving free cash flow generation, we don't expect Hanesbrands to continue being punished by the market. It had been one of the worst performing stocks in the S&P 500 in 2016, even as its top- and bottom-line performance marched steadily higher, and while we're not ignoring the company's exposure to a struggling retail environment (or its exposure to cotton costs), we view a good deal of its products (innerwear accounts for ~45% of sales) as borderline consumer staples, and its diversified geographic exposure helps mitigate risk associated with the current US retail space. No investment is ever perfect, and while we'll be watching its debt load, inventory movements and cash flow trends closely in coming years, we've added a 3% position in shares to the Dividend Growth Newsletter portfolio at $23.77 each.

Addressing the Intricacies of the Dividend Cushion Ratio

By Kris Rosemann and Brian Nelson, CFA



The Dividend Cushion ratio has proven to be an extremely useful tool for income investors to help safeguard their portfolios from dividend cuts, but it does have its limitations. Sometimes, external forces that cannot be captured in the calculation of the Dividend Cushion can impact the sustainability of the dividend payment. Some of these external factors can be as complex as a transformational acquisition, to as straightforward as an unexpected guidance reduction, to as simple as a capital allocation policy change. The board sets the size of the future dividend payment, and to put it bluntly, the board can do whatever it wants--regardless of the financial statements, provided it has the capital to do so.

Let's briefly walk through the calculation of the Dividend Cushion ratio. The Dividend Cushion ratio combines our forecasts of a company's traditional free cash flow generation (cash flow from operations less all capital spending) over the next five years with the company's last fiscal year net cash or net debt position. That sum is then divided by our projections of the company's cumulative cash dividend payments over the next five years--all housed in our discounted cash flow model. The projections are driven by analyst expectations, supported by management guidance and/or the underlying trajectory of the business in the near term (and cross checked against consensus numbers). In the out-years of the model (Years 3-5), assumptions are driven by a convergence to mid-cycle expectations on the basis of a normalized analytical approach or to capture ongoing secular long-term growth, in most cases.

Though a significant number of factors are reflected in a company's Dividend Cushion ratio via such financial assumptions, there are a number of situations that are difficult to anticipate as they often land outside the predictive nature of financial statement analysis. A recent example of this was the dividend

Please see *Addressing the Intricacies...*on next page

*Addressing the Intricacies...*from previous page

cut we witnessed at Diebold (DBD). Diebold's decision to cut its dividend was part of the company's capital allocation strategy laid out in its acquisition announcement of Wincor Nixdorf. Free cash flow had weakened in recent years, and the increased leverage the firm brought on to finance the deal ended up coming at the expense of the dividend. The company financed the cash portion of the deal with funds available and the sale of senior notes. A management team's unpredictable appetite for deal making can sometimes throw a wrench into our work, and while Quality Systems (QSII) was another instance, these situations are more the exception than the rule.

Another example came in July 2013 when Jakks Pacific (JAKK) suspended its dividend. The dividend cut came as a surprise to the market, and shares were pummeled. This sell-off was a result of a major "miss" in the firm's reported results and a rather large downward guidance revision. In this particular example, the issue was not a problem in the Dividend Cushion ratio process, but rather in the material change in the trajectory of Jakks Pacific's future business that management simply mis-estimated. The preferences of children had continued to move away from its more traditional leisure products and toward mobile device gaming. When management makes huge changes to its forward guidance with little warning, the Dividend Cushion ratio can be caught off guard. In Jakks' case, management's initial guidance was way off the mark, and this is something that's difficult to anticipate and falls outside the construct of the Dividend Cushion. This, unfortunately, happens.

Yet another instance occurred with National Oilwell Varco (NOV) in April 2016. This particular example, however, probably best falls into the category of: "the board can do what it wants." Although National Oilwell Varco's dividend cut had been directly related to expectations for continued pressure in the oil and gas markets, management cut its dividend significantly while it still had a solid Dividend Cushion ratio (and it still had a good one after the cut). In many ways, it should probably not have cut the dividend in the first place. That said, we can't really fault the firm for wanting to preserve cash in the then-difficult business environment, especially as year-over-year revenue trends looked extremely ominous at the time. Most companies cut their quarterly payout when the business is typically nearing a credit crunch, liquidity shortfall, or financial distress, but in case of National Oilwell Varco, things weren't that bad, and management overreacted. The ratio can't predict overcautious behavior by the board, a large unquantifiable dynamic.

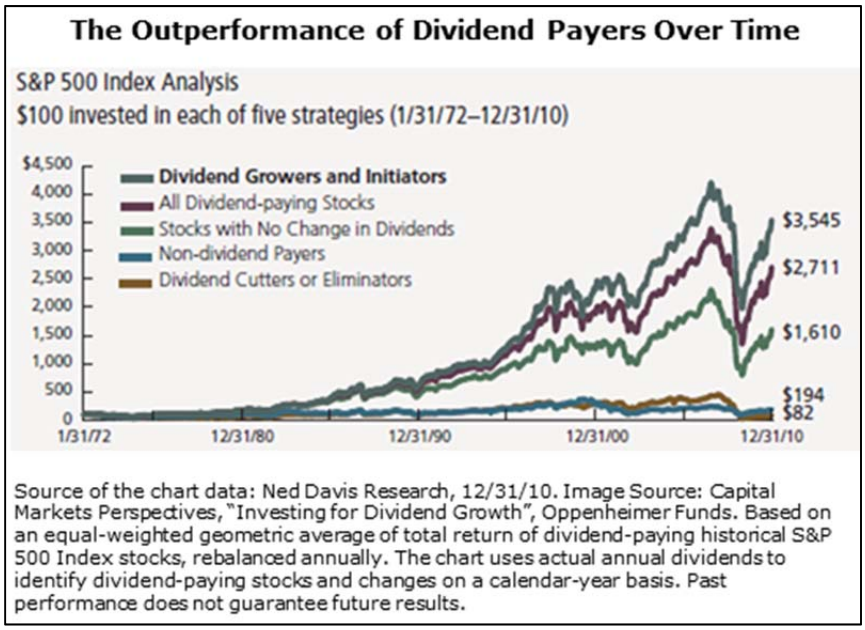
The latest example was Meridian Bioscience (VIVO). On January 25, the company cut its dividend after a rather large downward reduction in its own forward-looking assumptions, which it changed relatively suddenly. Similar to the case of Jakks above, for example, Meridian had just issued its guidance for 2017 in November, but just a few months later, the company abruptly cut its forecast for the entire fiscal year after only one quarter into the year. Clearly, we and the market were caught off guard, and management's unfounded optimism in November unfortunately found its way into the Dividend Cushion ratio. Making matters worse is that the earnings revision came at an inopportune time during our update process, as the next update to Meridian's dividend report was about to reflect the company's net balance sheet swing from a net cash position of ~$50 million at the end of 2015 to a net debt position of ~$10 million at the end of 2016 as a result of debt-financed M&A activity (a ~$60 million swing).

The Dividend Cushion ratio construct remains predictive but sometimes nuances can catch us off guard, as in the examples in this article. We're not happy about any of these instances, but we want to put them all on the table so that you can make the best use of the Dividend Cushion ratio. In many cases, knowing areas of weakness makes the process even stronger, and that's what we're hoping to achieve with this piece. Importantly, please always refer to the qualitative language found throughout the dividend reports for more in-depth and nuanced opinions of the quality of dividends in our coverage universe. We continue to work to improve our processes and add as much analysis regarding the strength or weakness of a company's dividend as possible within our research suite. Our updated reports on Meridian Bioscience are now available.

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 strongest 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) during tightening credit markets.

The Importance of Forward-Looking Dividend Analysis

Informed 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 more.

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

*About Our Valuentum Dividend Cushion…*from previous page

The Dividend Cushion Ratio Helps Income Investors

$$\frac{\sum_{t=1}^{5}[A(t) - B(t)] + C(0) - D(0)}{\sum_{t=1}^{5} E(t)}$$

A = cash flow from operations (from the operating section of the cash flow statement),
B = capital expenditures or additions to property plant and equipment (from the investing section of the cash flow statement),
C = cash and cash equivalents (from the balance sheet),
D = long-term debt (from the balance sheet), and
E = cash dividends paid (from the financing section of the cash flow statement).

"All else equal, a firm with billions of net cash on the balance sheet is better positioned to keep paying a dividend than a firm with billions of net debt on the balance sheet. More cash on the books relative to debt reveals significantly more financial flexibility. The dividend payout ratio ignores this important concept, while the Dividend Cushion ratio embraces it." – Valuentum's Brian Nelson, CFA

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.

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

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

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).

See more at the following link: http://www.valuentum.com/articles/20130528

The Valuentum Dividend Cushion Caught These Dividend Cuts in Advance

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

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

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

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

(3) Forecast adjusted to reflect Sunoco's poor free cash flow trends 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™ ratio 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™ ratio (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 6, Issue 2

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.

Image links:

Page 16:
https://twitter.com/realDonaldTrump/status/819550083742109696?ref_src=twsrc%5Etfw

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).

© Valuentum Securities, Inc. All rights Reserved. The information contained in this report is not represented or warranted to be accurate, correct, complete, or timely. This report is for informational and educational purposes only and should not be considered a solicitation to buy or sell any security. The securities mentioned herein may not be suitable for all types of investors. The information contained in this report does not constitute any investment advice, but especially on the tax consequences of making any particular investment decision. This material is not intended for any specific type of investor and does not take into account an investor's particular investment objectives, financial situation or needs.

This report is not intended as a recommendation of the securities highlighted or any particular investment strategy. Before acting on any information found in this report, readers should consider whether such an investment is suitable for their particular circumstances, perform their own due-diligence, and if necessary, seek professional advice. This report has not been tailored to suit any particular person's portfolio or holdings.

Assumptions, opinions, and estimates are based on our judgment as of the date of the report and are subject to change without notice. Valuentum is not responsible for any errors or omissions or for results obtained from the use of this report and accepts no liability for how readers may choose to utilize the content. In no event shall Valuentum be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of the information contained in this document. Investors should consider this report as only a single factor in making their investment decision. Redistribution is prohibited without written permission.

Valuentum is not a registered investment advisor, does not offer brokerage or investment banking services, and adheres to professional standards and abides by formal codes of ethics that put the interests of clients and subscribers ahead of their own. As of the date of this report, Valuentum has not received any compensation from companies highlighted in this report. Valuentum, its employees, and affiliates may have long, short or derivative positions in the stock or stocks mentioned herein.

No warranty is made regarding the accuracy of any data or any opinions. The portfolio in the Valuentum Dividend Growth Newsletter is unfunded and does not represent real money. Performance assessment of the Valuentum Buying Index™ is currently ongoing, and we intend to update investors as soon as such results are available. Past performance is not a guarantee of future results.

For general information about Valuentum's products and services, please contact us at info@valuentum.com.