Valuentum Securities, Inc. 1/2/2020 Edition 1, Volume 3

HIGH YIELD DIVIDEND NEWSLETTER

Here's to 2020!

Latest Changes to High Yield Dividend Newsletter
Previously Removed: 5% in AMLP – November 18
Previously Added: 2.5% to T; 2.5% to PM – November 18

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"THE GLOBAL MACROECONOMIC OUTLOOK IS IMPROVING IN PARTS OF THE WORLD, WITH CHINA'S OFFICIAL PMI COMING IN NORTH OF 50 IN NOVEMBER AND DECEMBER 2019. THAT HAS SUPPORTED MODESTLY HIGHER INTEREST RATES OF LATE, BUT SERIOUS HEADWINDS REMAIN." – CALLUM TURCAN

Image Shown: *Shares of VNQ, the Vanguard Real Estate ETF that invests primarily in real estate investment trusts ('REITs'), shot sharply upwards in 2019. That was primarily due to the US Fed switching (almost on a dime) from a trajectory of rising interest rates to falling interest rates.*

By Callum Turcan

Dear members,

We hope you all had a terrific holiday season with your family, friends, and loved ones. Looking ahead, we are excited for what 2020 has in store, especially for high yielding companies. The trajectory of interest rates and monetary policy will remain paramount heading into the new year. The US Fed has apparently become less dovish than before, relatively speaking. As of the December 2019 Federal Open Market Committee, the Fed was signaling that investors shouldn't expect a material change in monetary policy in 2020 (after cutting rates three times in 2019). **The Fed also signaled that interest rate increases aren't likely either in 2020, which is a big positive for high yielding firms.**

A while back, we covered National Grid plc (NGG) --- **4.9% yield** --- (6.2% yield back then, which declined due to capital appreciation) in the June 2019 edition of the High Yield Dividend Newsletter. In particular, as a utility with a lot of exposure to the UK, we cautioned that political risks (at the time) were quite severe. The leader of the UK Labour Party, MP Jermey Corbyn, sought to nationalize UK utilities and made that policy a platform of the Labour Party. While we noted that there's plenty to like about National Grid, those risks were hard to look past.

Fast forward to after the December 2019 general election in the UK, which saw the UK Tory Party trounce Labour. That loss encouraged MP Jermey Corbyn (who has led the Labour Party since 2015) to announce that he would be stepping down from being the leader of the party.

Shares of NGG shot upwards after the election results started rolling on in, and going forward, the outlook for National Grid looks quite promising. While Brexit remains an ongoing concern, the firm is well-positioned to handle what may come. In particular, we like National Grid's ability to earn a very attractive ROE at its various utility operations in the UK and the US.

Looking now at the High Yield Dividend Newsletter portfolio. HYDN portfolio holding CubeSmart (CUBE) --- **4.2% yield** --- raised its quarterly dividend by over 3% sequentially to $0.33 per share in December 2019. The self-storage company continues to perform well, and added 48 facilities to its third-party management platform during the third quarter of 2019.

While CubeSmart's management decided to modestly adjust the REIT's full-year guidance for 2019 to the downside on the net (on a company-wide basis), the firm reduced its estimated full-year weighted-average outstanding diluted share count for 2019. That allowed CubeSmart to actually raise its forecasted funds from operations ('FFO') guidance on a per share basis for 2019, from $1.66 - $1.69 per share previously to $1.67 - $1.69 per share as of its latest earnings report. **That implies CubeSmart is targeting a mid-to-high 70s% dividend payout ratio on an FFO basis in 2019, a reasonable level.**

CubeSmart is still expecting nice same-store revenue and net operating income ('NOI') growth in 2019, but expense growth is guided to be a bit stronger than previously expected. We continue to like CubeSmart as a top quality self-storage play with plenty of upside, especially as the firm can leverage its third-party management platform to find new facilities to acquire. Same-store occupancy rates averaged north of 93% in the third quarter of 2019.

Now turning to the Vanguard Real Estate ETF (VNQ) --- **3.8% yield** --- we continue to see a lot of value in having plenty of exposure to REITs. While recent changes in interest rate expectations have put a lot of pressure on REITs and other quasi-bond like investments, the global econony continues to face major headwinds going forward. Whether the nascent US-China semi-trade truce goes into effect and holds up is a big consideration, as is the slowing global economy with or without the US-China accord.

As the US Fed has signaled interest rate increases are unlikely in 2020, **REITs should benefit from high occupancy rates (due to the benign macroeconomic conditions in the US) and the ongoing low interest rate enviroment going forward.** What makes the VNQ ETF particularly appealing, and a key reason why we give shares of VNQ a heavier weighting in the HYDN portfolio, is its diversificaiton.

Looking at HYDN portfolio holding BP plc (BP) --- **6.5% yield** --- the energy giant should benefit from the IMO 2020 rules which are now in effect. The new maritime fuel regulators prohibit marine vessels from using fuel with sulfur content that exceeds 0.5%, which in theory should drive up demand for low sulfur diesel as bunker fuels that have high sulfur contents are tapped out (vessels with scrubbers can still use fuels with higher sulfur contents, like bunker fuels, but those scrubbers require relatively large upfront investments to install).

BP's downstream operations and marketing division should have the ability to profit off of this disruption while supplying IMO 2020 compliant fuels to the maritime industry

Disclosure: *Callum Turcan does not own shares of any of the securities mentioned above.*

AT&T Powers High Yield Dividend Newsletter Portfolio in 2019

By Brian Nelson, CFA

The high-yield dividend arena during 2019 was an exciting one, and we didn't sit on the sidelines. Avoiding mistakes was our modus operandi during 2019, and we did just that, but we landed a few big winners, too.

For starters, AT&T's (T) total return helped power the High Yield Dividend Newsletter portfolio higher, with a nice ~44% total return during the year. The iShares International Select Dividend ETF (IDV), as well as the iShares MSCI Australia ETF (EWA) also performed quite well, both advancing at a total return of ~22%-23%.

We view our blended benchmark in the high yield space as that of REITs and MLPs, and the MLPs suffered greatly during 2019, with the Alerian MLP ETF (AMLP) advancing a mere ~6% on a total return basis during the year. We have to say that we did quite well in this area, too, with our midstream MLP picks, Enterprise Products Partners (EPD) and Magellan Midstream Partners (MMP) leaping for a total return of ~22% and ~17% on the year, respectively, both returns a multiple of the AMLP's.

We continue to warn those investors navigating the MLP arena that it is fraught with business-model risk, but we're happy to see two of our favorites, EPD and MMP, in this treacherous area surge ahead.

Importantly, through the course of 2019, we didn't make any big mistakes in the High Yield Dividend Newsletter portfolio, and a good portion of our ideas outperformed the blended average of our benchmark, which we classify was the Vanguard Real Estate ETF (VNQ) and the AMLP. We're excited about what 2020 may bring to the high-yield dividend space, with the Fed now seemingly in-step with the markets, having cut rates a number of times during 2019.

All things considered, the High Yield Dividend Newsletter portfolio did great during 2019. We expect continued strong performance from AT&T as activist investors seek greater value creation, and it's hard for us not to like the diversification across both the core and equity portions of the portfolio. Philip Morris is one to watch in 2020, Public Storage may have a big year, and BP could deliver nicely along with rising crude oil prices. We're looking forward, and we like how the portfolio is positioned.

[Please see next page for a summary of portfolio activity during the year.]

Tracking the High Yield Dividend Newsletter	Price -- 12/31/2018 or at open*	Interim Dividends	Price -- 12/31/2019 or at close**
CORE			
Alerian MLP ETF (AMLP) -- *removed* November 18	8.73	0.78	7.83
Added 2.5pts of AT&T (T) -- November 18	*39.21*	-	39.08
Added 2.5pts of Philip Morris (PM) -- November 18	*84.57*	1.17	85.09
Global X SuperDividend ETF (SDIV)	17.10	1.54	17.69
Global X SuperIncome Preferred ETF (SPFF)	11.03	0.71	11.74
iShares International Select Dividend ETF (IDV)	28.71	1.73	33.57
iShares MSCI Australia ETF (EWA)	19.25	0.90	22.64
iShares U.S. Preferred Stock ETF (PFF)	34.23	2.00	37.59
Invesco Senior Loan Portfolio (BKLN)	21.78	1.11	22.82
ProShares High Yield -- Interest Rate Hedged (HYHG)	62.09	3.97	65.44
Utilities Select Sector SPDR (XLU) -- *added August 22*	*61.61*	0.99	64.62
Vanguard Real Estate ETF (VNQ) - *added April 1*	*85.91*	2.53	92.79
EQUITY			
AT&T (T)	28.54	2.04	39.08
BP PLC (BP)	37.92	2.46	37.74
CubeSmart (CUBE) -- *added August 22*	*35.13*	0.65	31.48
Digital Realty Trust (DLR)	106.55	4.32	119.74
Enterprise Products Partners (EPD)	24.59	1.76	28.16
Iron Mountain (IRM) -- *removed August 1*	32.41	1.22	29.97
Magellan Midstram Partners (MMP)	57.06	4.04	62.87
Omega Healthcare Investors (OHI) -- *removed March 1*	35.15	0.66	34.72
Philip Morris (PM) -- *added August 1*	*82.41*	2.34	85.09
Public Storage (PSA)	202.41	8.00	212.96
Schlumberger*, added January 18, removed August 1*	*43.00*	1.00	38.07
Realty Income Corporation (O) -- *removed April 1*	63.04	0.68	72.03
Tallgrass Energy LP (TGE) -- *removed August 1*	24.34	1.59	18.25

* As shown in the January 2019 edition of the High Yield Dividend Newsletter, or price at entry point

** Price as of December 31, 2019, or price at close

Americold Realty Trust is Heating Up

By Callum Turcan

One area that is starting to get more attention from investors concerns the refrigerated warehouse space. Americold Realty Trust (COLD) --- **2.3% yield** --- is one of the largest publicly traded real estate investment trusts ('REIT') that owns and operates temperature-controlled storage facilities. Please keep in mind Americold successfully went public in January 2018.

As of the end of September 2019, Americold operated over 175 cold storage warehouse facilities in the US, Australia, Canada, New Zealand, and Argentina. Please note most of Americold's facilities are in the US, and the firm owns the majority of its warehouses outright. Those facilities house over 1 billion in cubic feet of refrigerated storage space. Americold sold out of its Chinese joint-venture in 2019, which was a relatively small endeavor, for $15 million in cash proceeds.

The REIT operates under an umbrella partnership REIT ('UPREIT') structure as Americold Realty Operating Partnership L.P. owns substantially all of the assets and liabilities associated with the company. Americold Realty Trust owns 99% of the common general partnership interest in the operating partnership and is the sole owner of the general partner of the operating partnership. Also, the REIT's wholly-owned subsidiary Americold Realty Operations Inc, the only limited partner of the operating partnership, owns 1% of the common general partnership interest in the operating partnership. Americold also operates various taxable REITs and qualified REIT subsidiaries.

Americold has been transitioning from a model that relies on as-utilized, on-demand arrangements to one that's built on fixed storage commitments. This better allows Americold to manage its cash flow generation and provides for much more consistent revenue streams. Americold also offers value-added services to its customers including; foiling and netting, air and water tempering, meat boxing, allowing for on-site USDA inspections, date stamping, and more.

The REIT's goal is to connect agricultural and meat product producers to major distributors, retailers, and ultimately consumers. A key part of this strategy involves providing access to import and export facilities, and ensuring the relevant goods stay cool throughout the journey. Americold recently grew its footprint near a key US port, which we will cover later on in this piece.

What allowed Americold to transition to contracts based on fixed storage commitments, and away from less favorable arrangements, was the REIT's ability to cement itself as a leading cold storage supply chain solutions company. Scale allows Americold to offer better logistical services (some of its facilities are located near ports and major railroads, some near major consumer demand centers, and others near producers of agricultural and meat products) and connect buyers with sellers around the world (especially in the US).

Demand for cold storage facilities in the US should keep growing due to a few factors; rising produce consumption (data cited by Statista notes that per capita consumption of fresh fruit in the US rose by ~14% from 2000 to 2018, which combined with population growth supports an outlook for greater domestic fresh fruit consumption going forward), rising domestic produce production (forecasts from the USDA predict that US vegetable production by farm weight will grow by ~10% from 2017 to 2028), and rising usage of e-commerce grocery offerings.

Rising meat consumption in the US, largely a product of population growth, is another key consideration here. There's also upside to be had from greater US exports of agricultural and meat products.

As more and more Americans start to buy their groceries online, that will create logistical hurdles for e-commerce firms that seek to deliver fresh fruit, meat, vegetables, yogurt, and various frozen products (like ice cream) straight to the customer's door. Cold storage options are required to make e-commerce grocery services viable, especially when it comes to items like produce and meats which need to be kept cool constantly or they will spoil. Prepared frozen food, such as pizza or burritos, also needs to be kept cool constantly, as does milk.

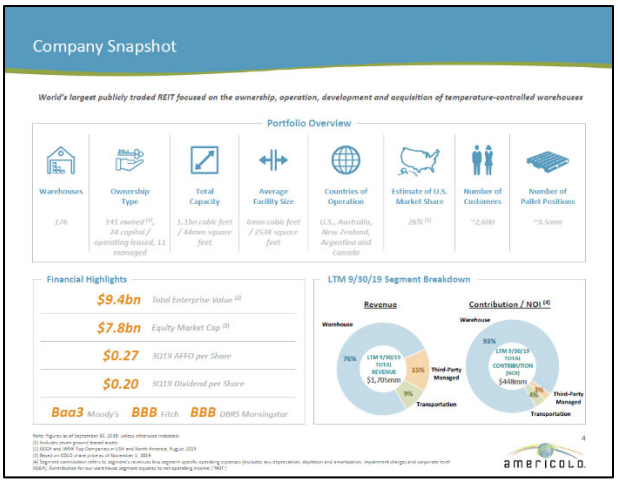

Image Shown: *An overview of Americold's asset base and financials.*
Image Source: *Americold – December 2019 IR Presentation*

For 2019, Americold is targeting same-store revenue growth of 2%-4% as its global warehouse segment, with same-store net operating income ('NOI') growth expected to be 100 – 200 basis points above that target. However, due to healthcare expenses coming in higher than expected, Americold sees its same-store NOI growth coming in at the low end of that range. The ability to increase the revenue and NOI generation capabilities of its existing assets speaks favorably towards Americold's outlook. Expansion and development-related capital expenditures are expected to come in at $205 million - $215 million in 2019, keeping in mind Americold is a very acquisitive company as well. Maintenance-related capital expenditures are estimated to be $50 million - $60 million in 2019.

In the third quarter of 2019, Americold's dividend coverage ratio defined under the REIT-specific term of adjusted funds from operations ('AFFO') per share divided by dividend per share, was ~74% (the goal is for the REIT to achieve a 64% - 68% AFFO payout ratio in 2019). That's decently below the 80% threshold we view as being necessary to retain a nice payout buffer, which we appreciate. Additionally, as Americold is capital market dependent, having an investment grade credit rating (Baa3/BBB/BBB) helps ensure the REIT can tap debt markets at attractive rates. Capital market dependence means that in order to maintain its business model and keep making good on its dividend obligations, Americold needs to issue equity and/or debt to raise funds.

Moody's (MCO) assigned an investment grade Baa3 (stable outlook) credit rating to the issuer rating of Americold's operating partnership in September 2019. Americold noted in its third quarter of 2019 earnings report that **this move effectively lowered the interest rate spread on its unsecured revolving credit line and unsecured term loan**. That speaks very favorably to Americold's ability to keep tapping capital markets at attractive rates in the foreseeable future. Here's what the REIT noted;

> *"Received Baa3/stable rating from Moody's, which reduced the Company's $800 million Unsecured Revolver spread by 55 basis points to L+90, and its $475 million Unsecured Term Loan A spread by 45 basis points to L+100."*

Americold generated $188 million in net operating cash flow in 2018 while spending $145 million on capital expenditures, **allowing for modest positive free cash flow. Furthermore, the REIT was free cash flow positive in both 2016 and 2017 as well.** Generally speaking, most REITs tend to generate negative free cash flow but less traditional REITs (like Americold or various public storage REITs) have shown strength on this front. Americold paid $87 million in distributions back to its parent in 2018 (due to the UPREIT structure), which required the REIT to tap capital markets to cover as its free cash flows fell short. Inclusive of short-term debt, Americold ended September 2019 with a net debt position of $1.4 billion. Having $0.3 billion in cash on hand on top of its revolving credit line provides Americold with ample liquidity and access to liquidity as needed.

In 2019, Americold acquired PortFresh Holdings (an operator of temperature-controlled storage facilities that cater to the Port of Savannah) for $36 million in cash and Lanier Cold Storage (its portfolio consisted of two temperature-controlled storage facilities in Georgia that will complement Americold's existing and future operations in the state) for $83 million in cash.

The PortFresh deal gave Americold better access to the fast growing port of Savannah in Georgia (providing better import and export options for its customers in North America) and the REIT plans to build a new 15 million cubic feet cold storage facility on the land acquired as part of the deal.

Management estimates the new facilities will cost between $55 million - $60 million to complete, with an operational in-service date targeted by the first quarter of 2020.

Americold also acquired Chiller Holdco which is known as Cloverleaf Cold Storage. The REIT paid over $1.2 billion in cash for the company, which was funded by equity issuance and from drawings on its revolving credit line. Cloverleaf had a portfolio of 22 cold storage facilities in the US, 21 of which were owned and one of which was managed. That deal closed in the second quarter of 2019. In a December 2019 press release, Americold announced it had completed its acquisition of two cold storage facilities and the underlying land for $54 million (one in Pennsylvania and one in Maryland) from a privately-held firm.

Furthermore, Americold agreed to acquire Nova Cold Logistics and its three temperature-controlled storage facilities in Canada for a bit over CAD$0.3 billion from Brookfield Business Partners (BBU), a deal that's expected to close in the first quarter of 2020. These acquisitions are giving Americold the kind of scale needed to be a serious player in the world of logistics. Gaining greater access to Canada's agricultural and meat industries and consumer demand centers reduces Americold's geographic concentration risk to a degree.

There's plenty to like about the cold storage space, and these are still very early days. Even though Americold is one of the largest publicly-traded firms in the space, its market capitalization only sits at ~$0.5 billion as of this writing. Clearly investors have taken a liking to the REIT as shares of COLD have roughly doubled since early-2018. **We appreciate its free cash flows, investment grade credit rating, growing asset base, and better arrangements with its customers (the shift towards fixed storage commitment contracts), but caution that Americold needs to retain constant access to capital markets to fund its growth trajectory.** Should capital markets freeze up, that would put tremendous stress on Americold's financials.

Disclosure: *Callum Turcan does not own shares of any of the securities mentioned above.*

-- THE HIGH YIELD DIVIDEND SPOTLIGHT IS ON THE NEXT PAGE --

High Yield Spotlight: Covering H&R Block Inc (HRB), a Tax Preparation Company Moving into New Ventures

Our Spotlight article for the January 2020 edition of the High Yield Dividend Newsletter portfolio will focus on US tax preparation firm **H&R Block** (HRB) --- **4.4% yield** --- which is headquartered in Kansas City, Missouri. We will highlight the idiosyncratic nature of H&R Block's seasonal financial performance over the course of its fiscal year, its strong free cash flow profile, and how a recent acquisition could augment its growth trajectory going forward.

H&R Block's financials can be a tricky read due to the very seasonal nature of its US tax preparation business, whether that be its assisted tax filing services or its do-it-yourself ('DIY') offerings. In fiscal 2019 (period ended April 30, 2019), H&R Block generated $0.6 billion in net operating cash flow. However, during the first half of fiscal 2019, H&R Block generated -$0.6 billion (negative $0.6 billion) in operating cash flow as most of the firm's business comes from the second half of its fiscal year.

Over the past three full fiscal years (fiscal 2017 to fiscal 2019), H&R Block generated ~$0.6 billion in free cash flow per fiscal year on average while its annual dividend obligations averaged ~$0.2 billion. Share buybacks are another consideration here, as is M&A activity which we'll cover in a moment. H&R Block repurchased a meaningful amount of its stock during this period, and those buybacks were lumpy.

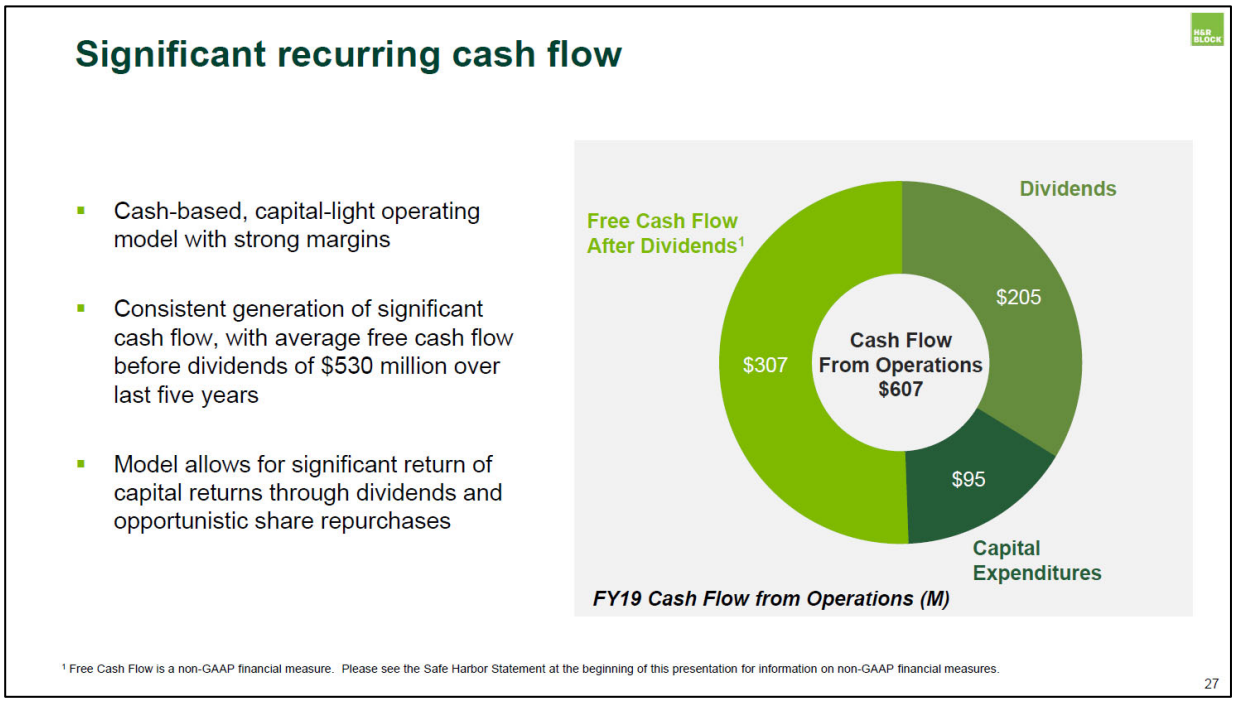

Image Shown: *H&R Block's free cash flow handily covered its dividend obligations in fiscal 2019.* ***Image Source:*** *H&R Block – December 2019 IR Presentation*

In fiscal 2019, H&R Block's tax preparation volume rose by just over 1% versus the previous fiscal year, aided by a 1.5% increase in the US. The firm's assisted US tax preparation volume declined by just under 2% year-over-year in fiscal 2019, however, H&R Block's paid US DIY tax preparation volume rose by almost 6%. Please note the US represents most of H&R Block's business.

The company also operates in Canada and Australia (along with an 'Other' category), but that doesn't represent much of its business (low double-digit percent in terms of total company-wide annual tax preparation volume).

In the upcoming two graphics, management highlights how assisted tax preparation offerings have held up well in terms of market share since the early-2000s. That being said, there is a slow but steady shift towards DIY options, which generally speaking are much cheaper. H&R Block launched its Tax Pro Go offering at the start of calendar year 2018 to cater to the middle ground, which offers remote tax preparation advice. Assisted US tax preparation services accounted for ~60% of H&R Block's revenues in fiscal 2019.

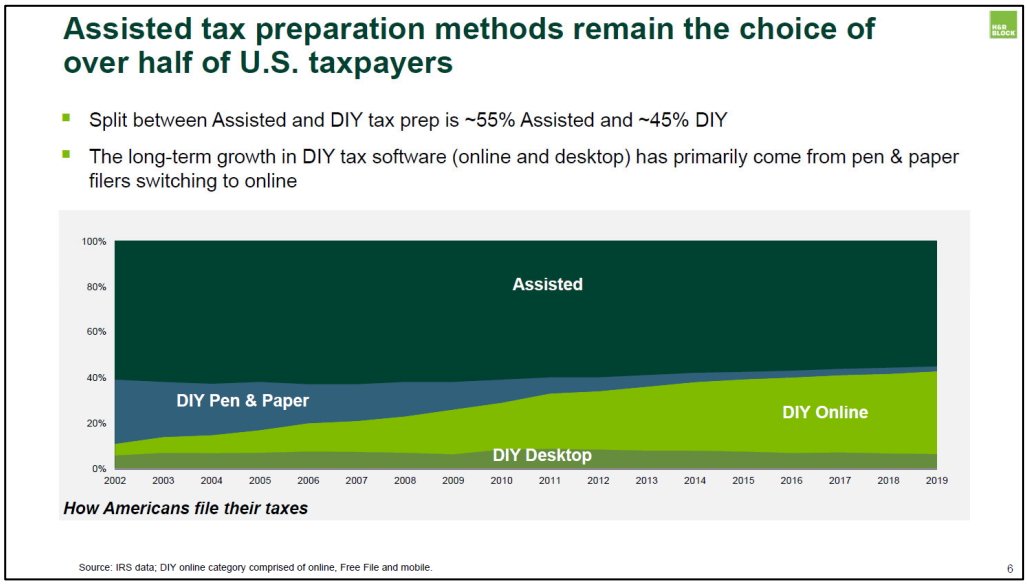

Image Shown: *Assisted US tax preparation services are still very popular in the US.* ***Image Source:*** *H&R Block – December 2019 IR Presentation*

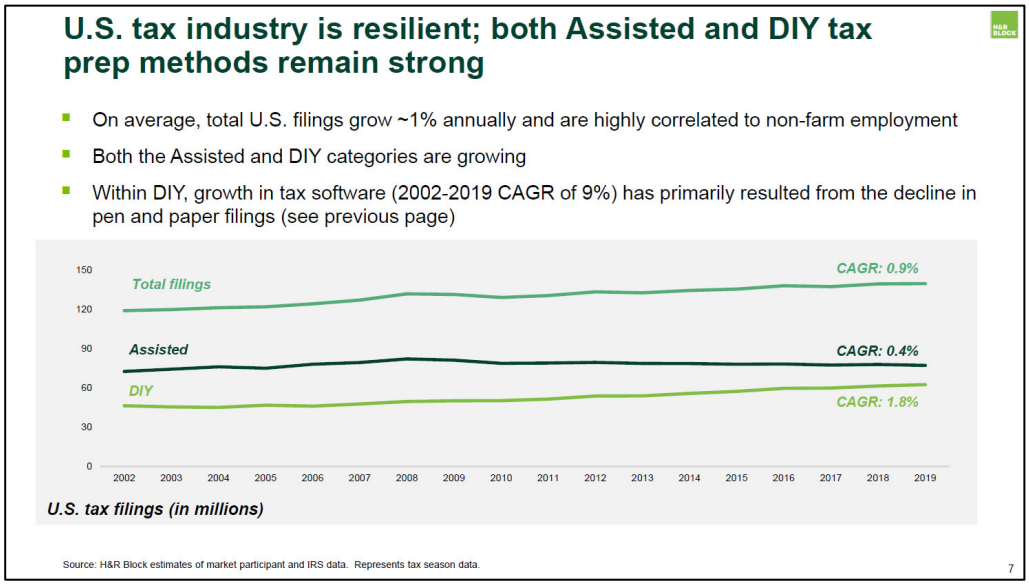

Image Shown: *While total US tax filings continue to grow at almost 1% per year, aided by growth in assisted US tax preparation services, it is clear DIY tax preparation offerings are taking market share.* ***Image Source:*** *H&R Block – December 2019 IR Presentation*

The company pushed through only a 1% increase in DIY net average charge in fiscal 2019 on an annual basis, while the net average charge at company-owned locations decreased 4%. H&R Block sought to lower the cost of its assisted tax preparation offering in part to stem the loss of business, while increases at its DIY offerings were very modest.

Going forward, growing popularity of its DIY tax filing offerings will potentially allow for meaningful increases in H&R Block's net average charge. Franchised operations saw a 2% year-over-year increase in net average charge in fiscal 2019, keeping in mind the net average charge of those operations is somewhat less than its company-owned locations (H&R Block receives royalties from those operations under franchise agreements). Please note that the net average charge of assisted US tax preparation services is substantially higher than the net average charge of DIY offerings by about seven-fold.

H&R Block's fiscal 2019 was rough due to the reduction in assisted tax preparation volume in the US and the reduced price of those offerings, which was made tougher by rising investments in its technology platform. There's room for optimism as management is expecting a turnaround in fiscal 2020. In fiscal 2019, H&R Block saw its GAAP revenues declined by 2% year-over-year.

In the middle of calendar year 2019, H&R Block acquired Wave Financial for $0.4 billion in cash, which was funded with its existing cash pile on hand. Wave Financial offers services geared towards small business owners that are intended to improve the financial processes of its clients including; free accounting, invoicing, and receipt-tracking software. The company is based in Toronto, Ontario, Canada, and generates revenue by selling such services as; payment processing, payroll services, and bookkeeping. Additional services are in the works, and that's before taking H&R Block's offerings into account.

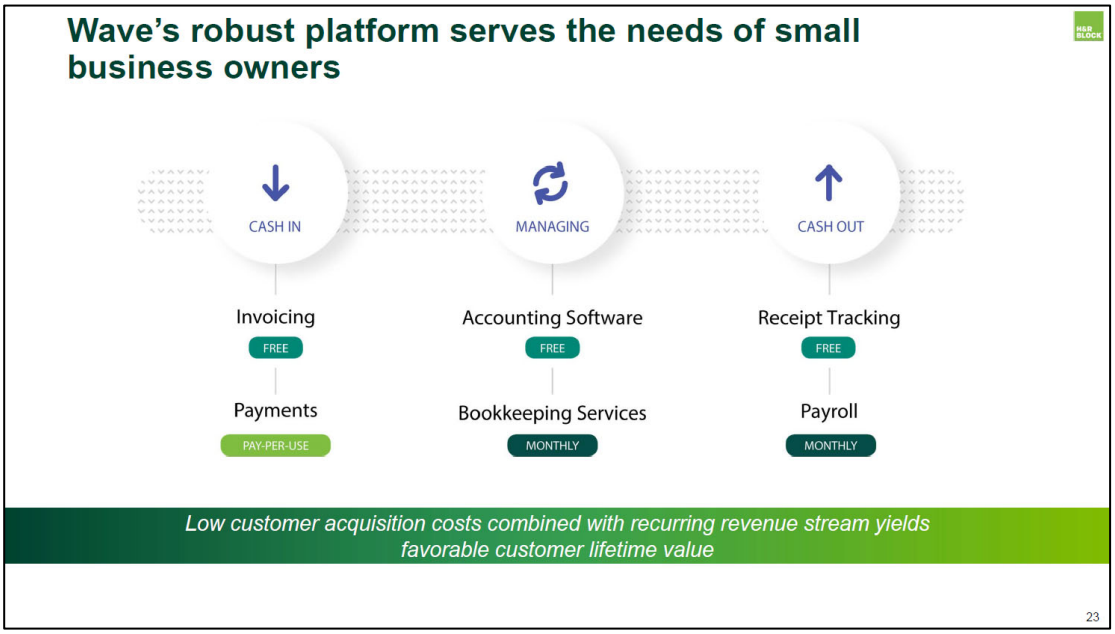

Image Shown: *A look at how Wave Financial, now a part of H&R Block, makes money while also offering free financial software.* ***Image Source:*** *H&R Block- December 2019 IR Presentation*

What H&R Block found so appealing about Wave Financial is the software firm's ability to acquire new customers at a low cost, meaning H&R Block can utilize the popularity of Wave Financial in the small business world to cross-sell that group tax preparation services. As of the middle of calendar year 2019, Wave Financial was catering to over 400,000 small businesses across the world every month.

There are obvious synergies here, and we are optimistic on H&R Block's ability to leverage this transaction to bolster its future financial performance. **Stronger revenue growth would go a long way in improving its free cash flow outlook, which already is solid due to its capital expenditure light business model.** Just as important, H&R Block is diversifying its business into adjacent areas within the realm of financial services. During H&R Block's second quarter fiscal 2020 conference call, management mentioned this;

> *"We are now emailing qualified H&R Block clients about Wave. We'll be emailing qualified Wave clients about H&R Block. So inside the installed base, we think there is a lot of opportunity that doesn't rely on a lot of incremental investment and that's where we're focused for fiscal '20."*

In the upcoming graphic, management provides their outlook for H&R Block's fiscal 2020 (a period that historically has ended in April). The firm is targeting modest revenue growth as the tax filing season returns to normal after the government shutdown last filing season, **with industry growth estimated to return to historical levels of ~1% according to management commentary.**

Detailed FY20 financial outlook

Revenue Growth	1.5% - 3.5%
EBITDA Margin[1]	24% - 26%
Effective Tax Rate	19% - 21%
Total Depreciation & Amortization	$165M - $175M
Acquisition Amortization[2]	*$70M - $80M*
Interest Expense	$90M - $100M
Capital Expenditures	$70M - $80M

[1] EBITDA and EBITDA Margin are non-GAAP financial measures. Specific quantifications of the amounts that would be required to reconcile the company's EBITDA Margin outlook for FY20 are not available. Because of the variability of these and other items as well as the impact of future events on these items, management is unable to reconcile without unreasonable effort the expected range of EBITDA Margin for the fiscal year to a comparable GAAP range. Please see the Safe Harbor Statement at the beginning of this presentation for information on non-GAAP financial measures.
[2] Acquisition Amortization includes amortization of intangibles related to Wave, franchise buybacks, and tax office acquisitions, and is included in Total Depreciation & Amortization.

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Image Shown: *H&R Block's outlook for fiscal 2020, and please note the firm's fiscal year historically ends in April.* ***Image Source:*** *H&R Block – Second Quarter Fiscal 2020 Earnings IR Presentation*

Additional upside will come from H&R Block's recent team up with Shopify Inc (SHOP). H&R Block is integrating with Shopify's App Store and should encourage greater usage of its tax filing services from Shopify's existing and future client base. Shopify's customer base of small- and medium-sized businesses are the kind of clientele that would likely want to use services provided by H&R Block and its new Wave Financial offerings. H&R Block has multiple credible avenues to juice its top-line growth, which supports its outlook.

In the upcoming graphic, H&R Block provides an overview of its credit rating as of the end of its fiscal 2019. **We appreciate its investment grade credit rating, as that indicates the company should retain access to capital markets at attractive rates.**

As of	April 30, 2019			April 30, 2018		
	Short-term	Long-term	Outlook	Short-term	Long-term	Outlook
Moody's	**P-3**	**Baa3**	**Negative**	P-3	Baa3	Stable
S&P	**A-2**	**BBB**	**Stable**	A-2	BBB	Stable

Image Shown: *H&R Block has an investment grade credit rating.* ***Image Source:*** *H&R Block – Fiscal 2019 Annual Report*

At the end of April 30, 2019, H&R Block was sitting on a net cash position of $0.1 billion (inclusive of short-term debt, which there wasn't any, and we aren't including restricted cash here). Due to the typical negative free cash flow expected during the first half of its fiscal year, on top of the cash acquisition of Wave Financial and $0.2 billion in share buybacks during this period, H&R Block's net cash position flipped to a $1.4 billion net debt position (inclusive of short-term debt) by October 31, 2019. Please note that this picture will very likely change materially by the end of April 2020 on the back of its expected free cash flows during the second half of fiscal 2020, as has historically been the case.

We will caution here that H&R Block did reduce its quarterly per share dividend, from $0.08 to $0.05, in late-1996 on a calendar year basis. Since then, adjusted for stock splits, H&R Block's dividend per share has grown substantially (without getting cut again), hitting $0.26 per share in calendar year 2019 on a quarterly basis. Most importantly, H&R Block's dividend survived the Great Financial Crisis intact. While the payout cut in the 1990s is a flag, that isn't a red flag given how H&R Block has changed substantially over the past 20+ years. Additionally, H&R Block has been paying out a common dividend since the 1970s.

Looking ahead, H&R Block's outlook is looking brighter. The company's free cash flow profile is solid, its dividend obligations are well-covered, we appreciate its investment grade credit rating, the firm's recent acquisition activity could reinvigorate top-line growth, and H&R Block has successfully found a way to offset pressures facing its assisted tax preparation business in the US by investing in its DIY offering and its technology platform more broadly.

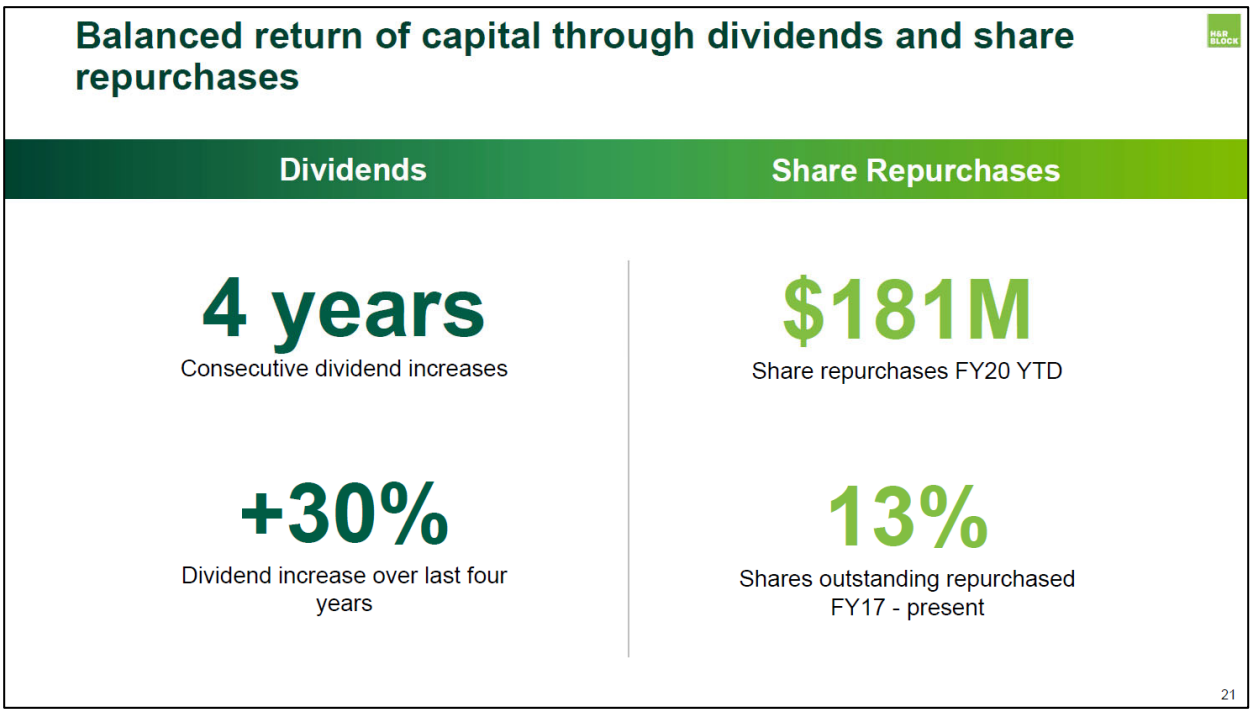


Image Shown: *H&R Block has historically been quite shareholder friendly, and we expect that should continue being the case going forward.* ***Image Source:*** *H&R Block – Second Quarter Fiscal 2020 Earnings IR Presentation*

Disclosure: *Callum Turcan does not own any of the securities mentioned above.*

Answering Member Questions -- VICI and DLR

Image Source: *VICI Properties Inc – November 2019 IR Presentation*

By Callum Turcan

<u>Member Question</u>: Is there any way to determine if REITs highlighted in the newsletters have exposure to the repo market? Those specifically are VICI and DLR?

Vici Properties Inc

November 2019 income generation idea VICI Properties Inc (VICI) --- **4.7% yield** --- is a unique real estate investment trust ('REIT') that owns top quality gaming and the related hospitality properties all across the US, with the rental revenues from those assets secured under long-term triple-net leases. **We like the REIT's free cash flows, business model, and well-managed financial position.**

Recently, we received a member question regarding whether VICI Properties was exposed to the ongoing turbulence in the repo market in light of the Fed pumping several hundred billion dollars' worth of liquidity into the banking system since September (the Fed's balance sheet has grown from ~$3.8 trillion in September 2019 to ~$4.1 trillion billion as of December 11, 2019) via repurchasing agreements according to *the WSJ*. That was to ensure liquidity levels remain flush and short-term lending rates are kept reasonable after suddenly spiking.

Overnight lending rates continue to pop upwards, and the Fed continues to intervene. Furthermore, the Fed has indicated that it intends to keep providing the market with liquidity as needed going forward to maintain stability and keep short-term lending rates in check.

In the two upcoming graphics down below, note that VICI Properties' debt load (as of the end of September 2019) doesn't start maturing until 2022 at the earliest. The need to refinance this burden is real, but it doesn't appear VICI Properties is exposed to the turbulence in the repo market. Additionally, capital markets at-large remain very willing to lend at attractive rates to many entities, including VICI Properties, which we will cover in just a moment.

In the two upcoming graphics down below, note that VICI Properties' debt load (as of the end of September 2019) doesn't start maturing until 2022 at the earliest. The need to refinance this burden is real, but it doesn't appear VICI Properties is exposed to the turbulence in the repo market. Additionally, capital markets at-large remain very willing to lend at attractive rates to many entities, including VICI Properties, which we will cover in just a moment.

Note 7— Debt

The following tables detail our debt obligations as of September 30, 2019 and December 31, 2018:

($ in thousands)	September 30, 2019			
Description of Debt	**Final Maturity**	**Interest Rate**	**Face Value**	**Carrying Value[1]**
VICI PropCo Senior Secured Credit Facilities				
Revolving Credit Facility [2]	2024	L + 2.00%	$ —	$ —
Term Loan B Facility [3]	2024	L + 2.00%	2,100,000	2,076,993
Second Lien Notes [4]	2023	8.00%	498,480	498,480
CPLV Debt				
CPLV CMBS Debt [5]	2022	4.36%	1,550,000	1,550,000
Total Debt			$ 4,148,480	$ 4,125,473

Image Shown: *VICI Properties' debt load, as of the end of September 2019, doesn't start maturing until 2022.* ***Image Source:*** *VICI Properties – Third Quarter 2019 10-Q Filing*

Down in the graphic below, please note that VICI Properties doesn't need to pay installments towards any tranche of its debt and can instead refinance that burden down the road just before maturity (or as management sees fit as VICI Properties has plenty of flexibility).

The following table is a schedule of future minimum payments of our debt obligations as of September 30, 2019:

(In thousands)	Future Minimum Payments
2019 (remaining)	$ —
2020	—
2021	—
2022	1,560,000
2023	520,480
2024	2,068,000
Total minimum repayments	$ 4,148,480

Image Shown: *VICI Properties' debt load, at the end of September 2019, didn't come with covenants requiring installment payments and can instead be refinanced just before maturity.* ***Image Source:*** *VICI Properties – Third Quarter 2019 10-Q Filing*

VICI Properties is an acquisitive company that's adding new gaming and hospitality properties to its operations all the time. The REIT completed its purchase of three gaming assets from Eldorado Resorts Inc (ERI) in December 2019 for $278 million in cash. Simultaneously when the deal closed, VICI Properties entered into a triple-net master lease agreement with Eldorado Resorts. Cash on hand was used to fund the deal. VICI Properties exited September 2019 with $431 million in cash and cash equivalents on hand, $343 million in short-term investments, and $32 million in restricted cash, providing it with ample liquidity.

Please note VICI Properties has other deals in the works which are set to close in 2020. To help fund these acquisitions, the REIT closed on issuing $1.25 billion in 4.25% Senior Notes due 2026 and $1.0 billion in 4.625% Senior Notes due 2029 in November 2019. A large part of those proceeds went towards refinancing $1.55 billion in debt secured by real estate, with the remaining proceeds going towards the relevant financing fees and more importantly, to fund upcoming transactions. Considering VICI Properties clearly retains access to capital markets at attractive rates and generally maintains a nice liquidity buffer on the balance sheet, the REIT's growth trajectory should be maintained through repo market turbulence of late.

On one final note, VICI Properties is very free cash flow positive. The firm generated $435 million in free cash flow during the first nine months of 2019 and spent $367 million on its dividend payments. VICI Properties' strong financials provides an enormous amount of support to its business model. Though the REIT can cover dividends with free cash flow, it still needs to maintain access to capital markets at attractive rates as excess free cash flow (after covering dividend obligations) isn't strong enough to build the kind of cash balance to simply retire its debt.

VICI PROPERTIES INC.
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
(In thousands, except share and per share data)

	September 30, 2019	December 31, 2018
Assets		
Real estate portfolio:		
Investments in direct financing and sales-type leases, net	$ 10,455,900	$ 8,916,047
Investments in operating leases	1,086,658	1,086,658
Land	94,711	95,789
Cash and cash equivalents	431,423	577,883
Restricted cash	32,087	20,564
Short-term investments	342,767	520,877
Other assets	137,920	115,550
Total assets	$ 12,581,466	$ 11,333,368
Liabilities		
Debt, net	$ 4,125,473	$ 4,122,264
Accrued interest	23,945	14,184
Deferred financing liability	73,600	73,600
Deferred revenue	250	43,605
Dividends payable	137,048	116,287
Other liabilities	147,081	62,406
Total liabilities	4,507,397	4,432,346
Commitments and contingencies (Note 10)		
Stockholders' equity		
Common stock, $0.01 par value, 700,000,000 shares authorized and 461,005,745 and 404,729,616 shares issued and outstanding at September 30, 2019 and December 31, 2018, respectively	4,610	4,047
Preferred stock, $0.01 par value, 50,000,000 shares authorized and no shares outstanding at September 30, 2019 and December 31, 2018	—	—
Additional paid-in capital	7,816,233	6,648,430
Accumulated other comprehensive loss	(77,116)	(22,124)
Retained earnings	246,587	187,096
Total VICI stockholders' equity	7,990,314	6,817,449
Non-controlling interest	83,755	83,573
Total stockholders' equity	8,074,069	6,901,022
Total liabilities and stockholders' equity	$ 12,581,466	$ 11,333,368

Image Shown: *A look at VICI Properties' balance sheet, keeping in mind plenty of transactions occurred in the fourth quarter of 2019 and are expected to occur going forward that will significantly change these figures.* ***Image Source:*** *VICI Properties – Third Quarter 2019 10-Q Filing*

Digital Realty Trust

Pivoting to Digital Realty Trust Inc (DLR) --- **3.6% yield** --- the data center REIT, a favorite holding in both our Dividend Growth Newsletter and High Yield Dividend Newsletter portfolios, we see the firm maintaining access to capital markets at attractive rates going forward. At the end of September 2019, Digital Realty had a negligible cash and cash equivalents balance on hand. However, its debt maturing within a year at that time is negligible as well. Digital Realty's maturities during the remainder of 2019 and for 2020 are immaterial, as you can see in the upcoming graphic at the top of the next page.

DIGITAL REALTY TRUST, INC. AND SUBSIDIARIES
DIGITAL REALTY TRUST, L.P. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)

proceeds from the offering were approximately €491.9 million (approximately $539.7 million based on the exchange rate on October 9, 2019) after deducting managers' discounts and estimated offering expenses. We used the net proceeds from the offering to repay borrowings outstanding under the operating partnership's global revolving credit facility and for other general corporate purposes.

The table below summarizes our debt maturities and principal payments as of September 30, 2019 (in thousands):

	Global Revolving Credit Facilities(1)	Unsecured Term Loans(1)	Senior Notes	Secured Debt	Total Debt
Remainder of 2019	$ —	$ —	$ —	$ 166	$ 166
2020	—	—	—	1,133	1,133
2021	—	—	—	—	—
2022	—	—	800,000	—	800,000
2023	1,652,546	799,533	718,670	104,000	3,274,749
Thereafter	193,480	—	6,730,377	—	6,923,857
Subtotal	$ 1,846,026	$ 799,533	$ 8,249,047	$ 105,299	$ 10,999,905
Unamortized discount	—	—	(17,578)	—	(17,578)
Unamortized premium	—	—	6,395	78	6,473
Total	$ 1,846,026	$ 799,533	$ 8,237,864	$ 105,377	$ 10,988,800

(1) The global revolving credit facility and 2024 Term Loan are subject to two six-month extension options exercisable by us. The bank group is obligated to grant the extension options provided we give proper notice, we make certain representations and warranties and no default exists.

Image Shown: *Digital Realty's near-term maturities are immaterial. It isn't until 2022 that significant tranches of the REIT's debt load start maturing.* ***Image Source:*** *Digital Realty – Third Quarter 2019 10-Q Filing*

It isn't until 2022 that Digital Realty has a significant amount of its current debt load coming due, just like VICI Properties. Also like VICI Properties, Digital Realty is an acquisitive company, meaning its balance sheet can change meaningfully from quarter-to-quarter. In October 2019, Digital Realty closed on €500 million of Euro-denominated 1.125% Guaranteed Notes due 2028, highlighting the REIT's ongoing ability to tap capital markets at attractive rates. However, unlike VICI Properties, Digital Realty was not free cash flow positive during the first nine months of 2019 and needs to retain access to capital markets to fund its dividend payments.

Digital Realty plans to merge with the European-focused data center REIT InterXion Holding NV (INXN) in an all-stock deal (INXN shareholders will own ~20% of the pro forma company's outstanding common shares, DLR shareholders will own the remainder). The $8.4 billion deal by enterprise value is expected to close in 2020, and "Digital Realty expects to refinance the Interxion debt assumed in the transaction with a combination of investment-grade corporate bonds and proceeds from other financings" which includes the $1.0 billion cash Digital Realty is raising from privately-held affiliates of Mapletree Investments Pte Ltd and Mapletree Industrial Trust (MAPIF) through a new joint-venture. Digital Realty is selling down its stake in various data center assets to the group, retaining a modest stake and operatorship of the venture going forward. The entire deal is expected to close by 2020 (the first portion closed in late-2019).

Please note that at the end of September 30, InterXion was sitting on €0.2 billion in cash and cash equivalents versus €1.25 billion in total debt (inclusive of negligible short-term borrowings). **A combination of recent Euro debt issuance proceeds and the closing of the two-part Mapletree deal should better allow for Digital Realty to easy refinance/retire debt taken on through the InterXion merger.** We don't think Digital Realty's growth story will be materially hampered by recent repo market turbulence. When it comes to near-term liquidity, Digital Realty can utilize its recent debt issuance proceeds, joint-venture proceeds, and the undrawn portion of its $2.35 billion global revolving credit line that was extended to January 2023 back in October 2018.

Concluding Thoughts

We love getting feedback from the Valuentum community and are more than happy to answer any questions from our members. VICI Properties and Digital Realty both retain access to capital markets at attractive rates, and both have quality financing strategies in place to fund their ongoing growth trajectories. The Fed has decided to combat repo market turbulence by providing the banking system with ample liquidity, which should ensure capital markets remain open and willing to lend (and that overnight lending rates are kept in check) going forward. We continue to like both VICI Properties and Digital Realty as income generation ideas.

Disclosure: *Callum Turcan does not own shares in any of the securities mentioned above.*

Searching for Dividend Plays Amongst the Next Six Regional Banks

By Matthew Warren

Previously, we looked at the big six banks in the US and the top 6 regional banks in search of potential yield plays and identified Wells Fargo (WFC) and KeyCorp (KEY) as banks with attractive dividend yields at the time of publication. In looking at the next 6 largest regional banks in this piece, you will see that we have identified another 4 high yielders, one of which we have written about previously in Comerica (CMA). We will highlight another bank, which we think is worth closer inspection in this piece.

It is worth reiterating right up front that a financial crisis and/or property price deflation of a certain magnitude can upset the apple cart when it comes to investing in bank stocks. When it comes to a situation like the Great Financial Crisis ('GFC') or something worse, banks as a group can come under a tremendous amount of pressure as revenues shrink, cost cutting past a certain point becomes difficult (especially as collection costs mount), and credit costs leap in dramatic fashion. **Many banks saw their credit costs go up five times in the GFC before receding.** Some shoddy banks saw their credit costs go up 10 or more times (so-called-normal) levels. The simple fact is that if credit costs go up high enough for the system, only the strongest banks have the earnings power and balance sheet to make it through to the other side without the risk of massive share dilution or bankruptcy. Don't forget that even the strongest of the large banks **WERE FORCED** by the US government to take on board capital during the GFC.

That's another thing: what is "normal" credit costs in the banking industry. Clearly, it depends on what lines of business a bank is in, what geographies it participates in, and the quality of the management teams' underwriting, amongst other things. All play key roles in determining where credit costs currently stand. **Pretty much all banks are currently telling investors that current credit losses are below "normal" and to expect "through the cycle" credit losses to be higher.**

Now with this comes the question of how many recessions to expect in a decade and how severe? If the answer is that the whole decade will be benign like the past one has then "normal" credit losses are lower, normalized earnings streams are higher, and banks are worth more. If the answer is that things like the GFC will come along more often, then weaker banks are at higher risk of permanent capital impairment and all banks are worth less on lower normalized earnings streams. No one can know for certain what will happen over the next decade.

So, what then is the most rational way to evaluate banks and then value the shares? To me, it makes sense to expect a couple normal sized recessions to come along each decade to determine normalized credit costs for the "through the cycle" figure. **It also does not make sense to speculate in very low-quality banks with little earnings power and weak balance sheets.** The reason being is that these banks can quickly fold if the big recession or depression comes along before any anticipated fundamental improvements. These **ARE NOT** double down bets. In fact, one can take this idea to the extreme and argue that almost or all banks are not double down bets due to the inherent financial leverage involved in the business model and the risk of a depression such as what took place in the 1930s recurring. In a depression, one must factor in things like depositor and funder confidence and the risk of bank runs. Things we began to see during the GFC. Even the strongest banks in the country must benefit from the confidence of others to keep operating at full capacity during a storm.

With regional banks a key question concerns geographical concentration risk (i.e. regional banks that are heavily exposed to US states with poor macroeconomic and demographic fundamentals). This is a major risk worth keeping in mind, as headline GDP growth figures for the US aren't necessarily reflective of the macroeconomic conditions facing the regional bank in question.

Having covered the worst-case scenarios in some detail, let's also not forget that many regional banks have been around for over a hundred years and have made it through all kinds of ridiculously difficult situations. Strong balance sheets, solid earnings power, and disciplined underwriting are the things to look out for when analyzing companies that operate within the banking and financial space.

So, let's jump into it. Below are the six next largest regional banks after the six we analyzed in our previous banking piece. In the upcoming graphic below, you can see the market capitalizations and forward dividend yields of these banks (the seventh to twelfth largest in the US):

		Share Price	Market Cap (B)	Forward Dividend	Yield
Fifth Third Bancorp	**FITB**	$ 30.75	$ 22.0	$ 0.96	3.1%
First Republic Bank	**FRC**	$ 117.80	$ 20.0	$ 0.76	0.7%
Citizens Financial Group	**CFG**	$ 40.65	$ 18.0	$ 1.44	3.6%
Regions Financial Corporation	**RF**	$ 17.23	$ 17.0	$ 0.62	3.6%
Huntington Bancshares	**HBAN**	$ 15.15	$ 16.0	$ 0.60	4.0%
Comerica	**CMA**	$ 71.82	$ 10.0	$ 2.68	3.8%

Image Source: *Yahoo Finance*

You will notice that all these yields are well north of the 30-year treasury bond, which has been trending towards ~2.4% in recent days. Shares of Huntington Bancshares (HBAN) lead the way with a ~4.0% yield, which is quite high by any standard. Shares of Comerica (CMA,) which we recently highlighted as a top tier bank, currently come with a ~3.7% dividend yield. Now, in the upcoming below graphic, you will see how well covered last year's dividends were at each of these banks:

		2018 EPS	2018 DPS	Div Coverage
Fifth Third Bancorp	**FITB**	$ 3.06	$ 0.74	414%
First Republic Bank	**FRC**	$ 4.81	$ 0.71	677%
Citizens Financial Group	**CFG**	$ 3.52	$ 0.98	359%
Regions Financial Corporation	**RF**	$ 1.36	$ 0.46	296%
Huntington Bancshares	**HBAN**	$ 1.20	$ 0.50	240%
Comerica	**CMA**	$ 7.20	$ 1.84	391%

Image Source: *Bank Annual Reports*

All these banks easily covered last year's dividend payments on an EPS basis, which helps explain why the projected dividends are higher in the current year. First Republic doesn't pay out much of its earnings because it benefits from rapid organic growth, which means that it must fund its asset growth with corresponding equity growth—either by retaining earnings, and it has also engaged in secondary share offerings to keep pace with its growth. For the rest of the banks, there is plenty of room for share buybacks on top of dividend payments. **Any bank investor concerned with dividend yields and potential dividend growth should also concern themselves with the earnings power of the banks being considered.**

So, let's look at the return on equity of these six regional banks below:

		2018 ROE
Fifth Third Bancorp	**FITB**	14.50%
First Republic Bank	**FRC**	10.90%
Citizens Financial Group	**CFG**	8.62%
Regions Financial Corporation	**RF**	10.33%
Huntington Bancshares	**HBAN**	13.40%
Comerica	**CMA**	15.82%

Image Source: *Bank Annual Reports*

Five out of six of these banks are earning above the roughly 10% cost of capital, and all six are doing so if you look at the return on tangible equity (excluding goodwill and intangibles.) Fifth Third (FITB), Regions Financial Corporation (RF), Huntington Bancshares (HBAN), and Comerica (CMA) **are all putting up return on tangible equity in the mid to upper teens—an impressive metric.** These levels of returns suggest two things to us: (a) these are some of the more competitively advantaged banks in our country, as compared to smaller and poorly run institutions and (b) this is a snapshot of a benign or good part of the banking cycle.

Another question we would recommend potential bank investors consider before looking for yield is whether these banks have healthy deposit franchises, as this speaks to the low-cost nature of the banks as well as the sustainability of their franchise and earnings power.

		2018 Loans	2018 Deposits	L/D Ratio	2018 Liabilities	Deposits/Total Liabilities
Fifth Third Bancorp	**FITB**	$ 93,876	$ 102,020	92%	$ 126,213	81%
First Republic Bank	**FRC**	$ 75,426	$ 79,063	95%	$ 90,527	87%
Citizens Financial Group	**CFG**	$ 116,660	$ 119,575	98%	$ 139,701	86%
Regions Financial Corporation	**RF**	$ 83,152	$ 94,491	88%	$ 110,307	86%
Huntington Bancshares	**HBAN**	$ 74,128	$ 84,774	87%	$ 97,679	87%
Comerica	**CMA**	$ 48,766	$ 55,935	87%	$ 63,311	88%

Image Source: *Banks Annual Reports*

These banks are very plain vanilla with deposits making up the vast majority of liabilities as opposed to capital markets borrowing – a sign of health. While some of the banks have nearly lent out their entire deposit base and are likely scratching around for deposit growth to keep up with asset growth, none of the banks have stretched past lending out all their deposits yet – another sign of reasonable health. The next question regarding the health of these banks is how well capitalized they are, which you can see in the below graphic:

		Common Tier 1 Ratio	Tangible common equity ratio
Fifth Third Bancorp	**FITB**	10.2%	8.7%
First Republic Bank	**FRC**	10.4%	7.1%
Citizens Financial Group	**CFG**	10.6%	9.0%
Regions Financial Corporation	**RF**	9.9%	7.8%
Huntington Bancshares	**HBAN**	9.7%	7.2%
Comerica	**CMA**	11.1%	9.8%

Image Source: *Banks Annual Reports*

In the previous graphic, you can see that all the banks are well capitalized. Their common equity Tier 1 ratios are a bit below the money center banks, but then they are not held to the same regulatory standards if they hold less than $100 billion in assets. The bank's allowance for bad loans is higher than the level of current write offs as well, reflecting a more normalized environment to come. We do not have any concerns about the level of bank's capital at this stage.

Aside from the safety of the dividend, the next question to ask is will it grow? Our view is that growth might slow going forward, as compared to the rear-view mirror of the past five years, though only time will tell.

		2014 Net Revenue	2018 Net Revenue	5 Yr Rev CAGR	2014 EPS	2018 EPS	5 Yr EPS CAGR	2014 Div	2018 Div	5 Yr Div CAGR
Fifth Third Bancorp	**FITB**	$ 6,073	$ 6,946	2.7%	$ 1.63	$ 3.06	13.4%	$ 0.51	$ 0.74	7.7%
First Republic Bank	**FRC**	$ 1,648	$ 3,044	13.1%	$ 3.07	$ 4.81	9.4%	$ 0.54	$ 0.71	5.6%
Citizens Financial Group	**CFG**	$ 4,979	$ 6,128	4.2%	$ 1.55	$ 3.52	17.8%	$ 1.43	$ 0.98	-7.3%
Regions Financial Corporation	**RF**	$ 5,064	$ 5,754	2.6%	$ 0.78	$ 1.36	11.8%	$ 0.18	$ 0.46	20.6%
Huntington Bancshares	**HBAN**	$ 2,816	$ 4,510	9.9%	$ 0.72	$ 1.20	10.8%	$ 0.21	$ 0.50	18.9%
Comerica	**CMA**	$ 2,512	$ 3,328	5.8%	$ 3.16	$ 7.20	17.9%	$ 0.79	$ 1.84	18.4%

Image Source: *Bank Annual Reports*

In terms of earnings per share, all of these banks stand out with double-digit earnings growth or better. Citizens and Comerica have made the most improvement over the past five years. **With net interest margin pressure ahead from Federal Reserve rate cuts and some flattening of the yield curve, the next year might augur slower revenue growth, but that depends on where the economy goes too.** Now let's look at loan and deposit growth, which drives the P&L.

		2014 Loans	2018 Loans	5 Yr Loans CAGR	2014 Deposits	2018 Deposits	5 Yr Deposit CAGR
Fifth Third Bancorp	**FITB**	$ 91,127	$ 93,876	0.6%	$ 93,477	$ 102,020	1.8%
First Republic Bank	**FRC**	$ 37,602	$ 75,426	14.9%	$ 37,131	$ 79,063	16.3%
Citizens Financial Group	**CFG**	$ 93,410	$ 116,660	4.5%	$ 95,707	$ 119,575	4.6%
Regions Financial Corporation	**RF**	$ 77,307	$ 83,152	1.5%	$ 94,200	$ 94,491	0.1%
Huntington Bancshares	**HBAN**	$ 47,051	$ 74,128	9.5%	$ 51,732	$ 84,774	10.4%
Comerica	**CMA**	$ 48,593	$ 50,163	0.6%	$ 54,784	$ 55,935	0.4%

Image Source: *Bank Annual Reports*

In terms of loan growth, First Republic and Huntington really stand out. First Republic is growing especially amongst a wealthier client set and Huntington benefitted from its acquisition of FirstMerit. Both banks grew deposits even faster than loans – a very healthy sign.

Conclusion

As mentioned previously, we highlighted Comerica as a nice income generating opportunity in a previous piece written for this publication and we are reiterating that view today. The other three banks that are worth a closer inspection based simply on the potential to pick up yield are Citizens, Regions, and Huntington.

Of these, Huntington Bancshares looks the most promising with its outstanding growth over the past five years (albeit bolstered by the acquisition of FirstMerit). It also appears to be on a good trend regarding its efficiency ratio, which bodes well for maintaining or increasing its already impressive return on capital ratios. Please note the strength of Huntington's financials over the past several years, and the many improvements the firm has made during this period, in the upcoming graphic at the top of the next page.

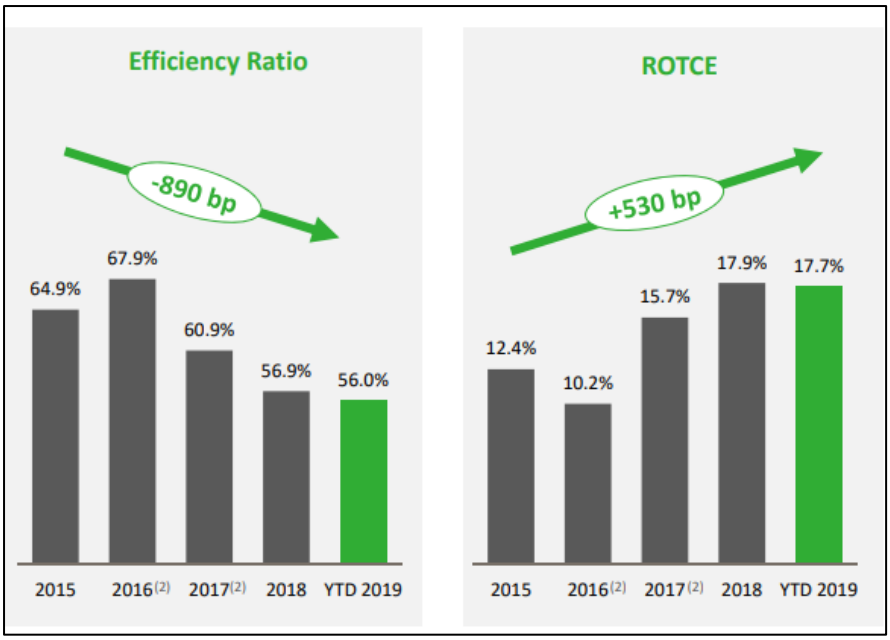


Image Source: *Huntington Bancshares – December 2019 Presentation*

We will take that closer look in future write ups, but for now, please keep in mind that the only thing we find concerning about Huntington is that its footprint is in the industrial rust belt of the Midwest and eastwards. This particular geographical exposure could act as a brake on organic growth and could spell trouble for credit costs should a very sizable downturn in the economy materialize. That being said, there's plenty of earnings power and balance sheet strength to soak up any pain that comes down the road. HBAN's ~4.0% yield is enticing.

Disclosure: *Matthew Warren does not own shares in any of the securities mentioned above.*

Key Contributors

- Brian Nelson, CFA
President, Investment Research
brian@valuentum.com

- Callum Turcan
Associate Investment Analyst
info@valuentum.com

- Matthew Warren
Independent Contributor
info@valuentum.com

Disclosure: *Brian Nelson, Callum Turcan, and Matthew Warren do not own any shares of any securities mentioned in their authored articles. Please contact info@valuentum.com for more information regarding Valuentum's editorial policies.*

THE SIMULATED HIGH YIELD DIVIDEND NEWSLETTER PORTFOLIO

We can't begin to tell you how excited we continue to be about the high yield space. We think we did pretty good the past few years given the uncertainty regarding Fed policy, and as you've noticed since the December 2018 bottom in the market, high yield dividend equities have come roaring back!

We think this is the beginning of what could be a nice run in the space given a more "dovish" stance by Fed policy. We also think the High Yield Dividend Newsletter portfolio positions us fairly well for whatever the market may throw at us. We're pretty well-diversified, and we've started to identify some pretty good individual equity ideas of late.

The high yield dividend equity arena trades a lot like junk bonds, meaning that interest rates play a key role in how equities will perform. As interest rates fall, high yield stays in vogue, but as interest rates rise, many look elsewhere. This impacts pricing greatly.

We're laser focused on identifying high yielding stocks that have sustainable yields, and if the income stream becomes threatened, we won't hesitate to say goodbye to a name. The High Yield Dividend Newsletter portfolio is presented each month in similar fashion (list and weightings) as that of the first edition.

If you have any questions, comments, or concerns, please be sure to let us know at info@valuentum.com.

Idea	Symbol	Weighting	Est Div Yield
CORE			
Global X SuperDividend ETF	SDIV	5.0%	9.16%
Global X SuperIncome Preferred ETF	SPFF	10.0%	6.29%
iShares International Select Dividend ETF	IDV	5.0%	5.60%
iShares MSCI Australia ETF	EWA	5.0%	5.21%
iShares U.S. Preferred Stock ETF	PFF	5.0%	5.63%
PowerShares Senior Loan Portfolio	BKLN	5.0%	5.17%
ProShares High Yield—Interest Rate Hedged	HYHG	5.0%	6.25%
Utilities Select Sector SPDR	XLU	5.0%	2.96%
Vanguard Real Estate ETF	VNQ	10.0%	3.12%
EQUITY			
AT&T	T	7.5%	5.32%
BP PLC	BP	5.0%	6.52%
CubeSmart	CUBE	5.0%	4.19%
Digital Realty Trust	DLR	5.0%	3.61%
Enterprise Products Partners	EPD	5.0%	6.29%
Magellan Midstream Partners	MMP	5.0%	6.49%
Philip Morris	PM	7.5%	5.50%
Public Storage	PSA	5.0%	3.76%
Cash*	-	0.0%	1.75%
		100.0%	**5.29%**

This is not a real money portfolio. Inception 1/1/2018. Data as of 12/2/2019. Est. Div. Yield retrieved from YahooFinance.

** Reflects high end of federal funds rate range*

SCREEN OF THE MONTH – THE FINANCIALLY-HEALTHIEST DIVIDEND PAYERS YIELDING OVER 2%

The following is a list of stocks that have the highest multiplicative combination of their dividend yield and Dividend Cushion ratio, per our estimates. We exclude the business models of master limited partnerships and real estate investment trusts in this screen and focus exclusively on corporates. We also make a few other tweaks with respect to business model risk considerations.

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 overlaid the screen with an Economic Castle assessment to consider business-model risk, too!

Note: *The 'Multiple' in this list considers a company's dividend yield and Dividend Cushion ratio as a multiplicative combination. Though it is a robust and largely objective measure, there could be exogenous or secular dynamics that could impact the business, where a dividend may not be as strong as the financials indicate.*

Company Name	Symbol	Sector	Div Yield	Economic Castle	Multiplier
General Motors	GM	Consumer Discretionary	4.1%	Attractive	14.13
Honda	HMC	Consumer Discretionary	3.9%	Neutral	13.94
Gilead Sciences	GILD	Health Care	3.9%	Very Attractive	12.17
Fluor	FLR	Industrials	2.9%	Attractive	11.79
Guess	GES	Consumer Discretionary	2.7%	Attractive	11.33
Lear Corp	LEA	Consumer Discretionary	2.8%	Attractive	10.98
Hewlett-Packard	HPQ	Information Technology	3.7%	Attractive	10.84
Bristol-Myers Squibb	BMY	Health Care	2.9%	Very Attractive	10.29
Gap	GPS	Consumer Discretionary	6.0%	Attractive	10.25
Ralph Lauren	RL	Consumer Discretionary	2.8%	Attractive	10.08
Tapestry	TPR	Consumer Discretionary	5.2%	Attractive	9.95
Methode Electronics	MEI	Information Technology	1.6%	Attractive	9.75
Automatic Data Processing	ADP	Information Technology	2.8%	Very Attractive	9.70
Total	TOT	Energy	5.6%	Neutral	9.10
Cisco	CSCO	Information Technology	3.2%	Very Attractive	8.58
Cheesecake Factory	CAKE	Consumer Discretionary	3.7%	Attractive	8.52
Ethan Allen	ETH	Consumer Discretionary	4.9%	Unattractive	8.21
Dick's Sporting	DKS	Consumer Discretionary	3.0%	Attractive	7.96
QUALCOMM	QCOM	Information Technology	3.6%	Very Attractive	7.71
H&R Block	HRB	Consumer Discretionary	3.7%	Very Attractive	7.67
AVX Corp	AVX	Information Technology	2.5%	Attractive	7.50
Ford	F	Consumer Discretionary	6.5%	Neutral	7.47
Archer-Daniels-Midland	ADM	Consumer Staples	3.5%	Attractive	7.40
Novartis	NVS	Health Care	3.1%	Attractive	7.27
MKS Instruments	MKSI	Information Technology	0.8%	Attractive	7.15
Caterpillar	CAT	Industrials	2.9%	Very Attractive	7.14
Applied Materials	AMAT	Information Technology	2.0%	Very Attractive	7.01
McKesson	MCK	Health Care	1.2%	Very Attractive	6.99
Harley-Davidson	HOG	Consumer Discretionary	4.2%	Attractive	6.97
Cardinal Health	CAH	Health Care	4.2%	Attractive	6.95
Manpower	MAN	Information Technology	2.3%	Attractive	6.92
AmerisourceBergen	ABC	Health Care	2.0%	Very Attractive	6.92
Apple	AAPL	Information Technology	1.3%	Highest Rated	6.91
Walgreens Boots Alliance	WBA	Consumer Staples	3.1%	Attractive	6.81
Altria Group	MO	Consumer Staples	6.7%	Very Attractive	6.78
Robert Half	RHI	Information Technology	2.0%	Very Attractive	6.77
British American	BTI	Consumer Staples	6.9%	Unattractive	6.74
Amgen	AMGN	Health Care	2.6%	Very Attractive	6.74
Pfizer	PFE	Health Care	3.9%	Attractive	6.71
KLA-Tencor	KLAC	Information Technology	2.4%	Very Attractive	6.69
Xerox	XRX	Industrials	3.2%	Attractive	6.69
Expeditors Intl	EXPD	Industrials	1.4%	Very Attractive	6.63
Cedar Fair	FUN	Consumer Discretionary	6.7%	Attractive	6.62
Garmin	GRMN	Industrials	2.9%	Attractive	6.59
Johnson & Johnson	JNJ	Consumer Staples	2.8%	Attractive	6.54
Hillenbrand	HI	Consumer Discretionary	2.5%	Attractive	6.52
Paychex	PAYX	Information Technology	2.9%	Very Attractive	6.49
Taiwan Semiconductor	TSM	Information Technology	3.2%	Attractive	6.48
AstraZeneca	AZN	Health Care	3.0%	Attractive	6.42
MSC Industrial	MSM	Industrials	4.0%	Attractive	6.26

Note: The 'Multiple' in this list considers a company's dividend yield and Dividend Cushion ratio as a multiplicative combination. Though it is a robust and largely objective measure, there could be exogenous or secular dynamics that could impact the business, where a dividend may not be as strong as the financials indicate.

For example, there may be stocks that are dealing with a secular shift toward digital consumption or navigating changing consumer preferences as millennials seek 'experiences' not 'things' (e.g. fashion). These may not be the best dividend growth stocks to consider. The Dividend Cushion is only one factor that we use in assessing the overall health of a company's dividend.

DIVIDEND REPORT PAGE 2 – SEAGATE TECHNOLOGY PLC (STX)

Seagate STX FAIRLY VALUED

Buying Index™ 6 **Value Rating**

Economic Castle	Stock Fair Value Range	Dividend Track Record	Dividend Safety / Cushion™	Div Growth Potential	Dividend Yield
Very Attractive	$38.00 - $70.00	RISKY	GOOD / 1.3	POOR	4.37%

Assessment of Company Dividend Strategy

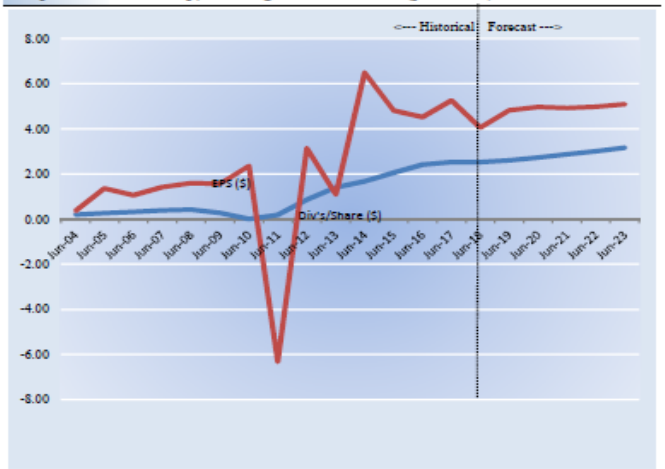
Key Strengths

Seagate had to cut its dividend during the Financial Crisis to "enhance liquidity," and it may have to do so again if right-sizing its operations does not go smoothly. The company's substantial leverage may put it at a disadvantage versus rivals, but more pointedly, it poses a direct threat to the health of its payout. A substantial portion of operating cash flow is directed toward debt-service costs, and its cash reserves and operating cash flow continue to dwindle. Sustaining the dividend at present levels could be a challenge. but the company has done well in generating ample free cash flow in recent years. This is not always the case in its dynamic and cyclical end market, a characteristic that exacerbates the risks associated with its financial leverage.

Potential Weaknesses

Seagate is beholden to the fast-changing, short-term dynamics of the data storage market, which are not conducive for long-term dividend growth. The company is a prime example of this as it was forced to cut its payout in fiscal 2009. Threats from the cloud and declines in PC sales pose direct secular threats to Seagate's business (even if such trends drive growing 'Exabyte' demand), and pricing competition within its consolidating industry (Western Digital bought SanDisk) will never truly ease, in our view. Its total debt load stood at ~$4.8 billion as of the end of fiscal 2018. The company's recently announced restructuring plan and job cuts should result in nice annual savings, but they are signs of distress in the business.

Graphical Relationship, Earnings and Dividends (per share)

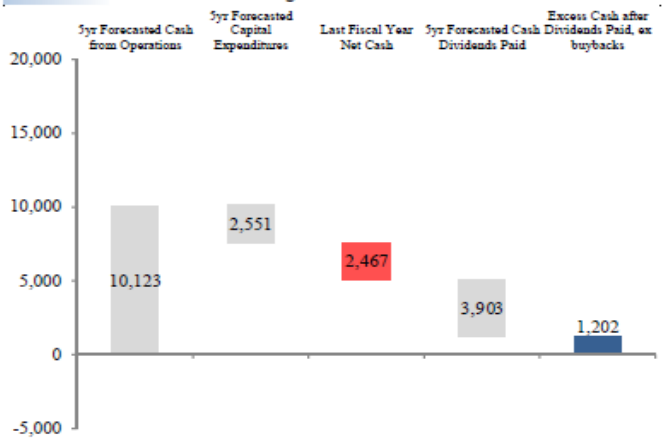


The graph above shows the relationship between a firm's earnings per share and its dividends per share.

Dividend Cushion Cash Flow Bridge Evaluation

The Dividend Cushion Cash Flow Bridge, shown in the image to the right, illustrates the components of the Dividend Cushion ratio and highlights in detail the many drivers behind it. Seagate's Dividend Cushion Cash Flow Bridge reveals that the sum of the company's 5-year cumulative free cash flow generation, as measured by cash flow from operations less all capital spending, plus its net cash/debt position on the balance sheet, as of the last fiscal year, is greater than the sum of the next 5 years of expected cash dividends paid. Because the Dividend Cushion ratio is forward-looking and captures the trajectory of the company's free cash flow generation and dividend growth, it reveals whether there will be a cash surplus or a cash shortfall at the end of the 5-year period, taking into consideration the leverage on the balance sheet, a key source of risk. On a fundamental basis, we believe companies that have a strong net cash position on the balance sheet and are generating a significant amount of free cash flow are better able to pay and grow their dividend over time. Firms that are buried under a mountain of debt and do not sufficiently cover their dividend with free cash flow are more at risk of a dividend cut or a suspension of growth, all else equal, in our opinion. Generally speaking, the greater the 'blue bar' to the right is in the positive, the more durable a company's dividend, and the greater the 'blue bar' to the right is in the negative, the less durable a company's dividend.

Dividend Cushion Cash Flow Bridge

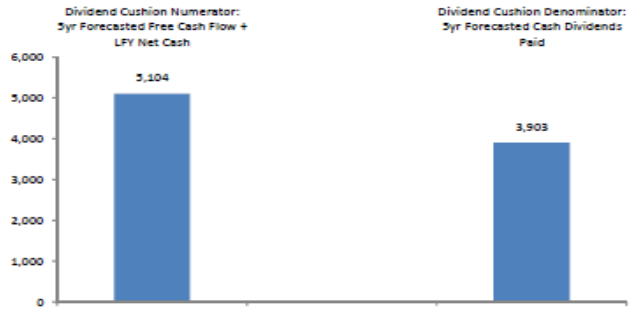


Source: Company Filings, Valuentum Projections

Dividend Cushion Ratio Evaluation

The Dividend Cushion Ratio Deconstruction, shown in the image to the right, reveals the numerator and denominator of the Dividend Cushion ratio. At the core, the larger the numerator, or the healthier a company's balance sheet and future free cash flow generation, relative to the denominator, or a company's cash dividend obligations, the more durable the dividend. In the context of the Dividend Cushion ratio, Seagate's numerator is larger than its denominator suggesting strong dividend coverage in the future. The Dividend Cushion Ratio Deconstruction image puts sources of free cash in the context of financial obligations next to expected cash dividend payments over the next 5 years on a side-by-side comparison. Because the Dividend Cushion ratio and many of its components are forward-looking, our dividend evaluation may change upon subsequent updates as future forecasts are altered to reflect new information.

Dividend Cushion Ratio Deconstruction



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DEFINITIONS

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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).

ValueTrend. This is a proprietary Valuentum measure. ValueTrend indicates the trajectory of the firm's return on invested capital (ROIC). Firms that earned an ROIC last year that was greater than the 3-year average of the measure earn a POSITIVE rating. Firms that earned an ROIC last year that was less than the 3-year average of the measure earn a NEGATIVE rating.

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