

BEATING THE TSX – IT WORKS!

TORONTO CMS CONFERENCE



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I GAVE MY FIRST CMS TALK HERE IN 1997, 16 YEARS AGO. YET, THE TITLE AND THE OUTLINE ARE THE SAME AND SO IS THE MESSAGE.

OUTLINE

- 1-WHY SHOULD I INVEST AT ALL?
- 2-IN WHAT SHOULD I INVEST?
- 3-WHY INVEST IN BIG-CAP CANADIAN STOCKS?
- 4-HOW CAN I INVEST IN DIVIDEND STOCKS?
- 5-HOW DOES 'BEATING THE TSX' WORK?
- 6-HOW HAS 'BEATING THE TSX' PERFORMED?
- 7-WHAT IS THE DOWNSIDE RISK?

1. WHY SHOULD I INVEST? A. DEMOGRAPHICS:

AGING CANADIAN POPULATION, % of 60+ BY 2050 WILL INCREASE FROM 21 TO 31%; LIFE EXPECTANCY—2011 (M+F) = 81.4, BUT, DISEASE-FREE = 68.6; LONGER RETIREMENT—AVG. RET. AGE ~62. YOU WILL NEED TO FUND A LONGER LIFE. WON'T BE ENOUGH PEOPLE WORKING TO FUND RETIREMENTS FOR FUTURE GENERATIONS. NEED TO INVEST TO FUND YOUR LONGER LIFE AND LONGER RETIREMENT.

B. OTHER REASONS TO INVEST:

SEND THE KIDS TO SCHOOL; ENABLE A LARGE PURCHASE, e. g. , A HOUSE; LEAVE SOMETHING TO YOUR HEIRS; BUY BACK SOME TIME FROM YOUR EMPLOYER. WEALTH CREATION BY INVESTING ALLOWS FOR FREEDOM TO SPEND TIME WITH GRANDKIDS, DONATE TIME TO CHARITY, ETC. INVESTING ALLOWS YOU TO BECOME FREE, TO REGAIN YOUR TIME, TO DO THE THINGS YOU BELIEVE HOLD MEANING.

2-IN WHAT SHOULD I INVEST?

HISTORICALLY, A MIXTURE OF COMMON STOCKS AND FIXED-INCOME PRODUCTS GIVE THE BEST AND SAFEST RETURNS. BUT YOU, AND ONLY YOU, MUST PICK THAT RATIO THAT FITS YOU BEST, TAKING INTO ACCOUNT: AGE, TNW, RISK TOLERANCE, DEBT LOAD, HEALTH, PENSIONS, JOB SECURITY, EARNING PROSPECTS, POSSIBLE INHERITANCES, FAMILY RESPONSIBILITIES, AND MANY OTHER FACTORS.

ARE THERE ANY 'SAFE' INVESTMENTS? SURE, YOU CAN PURCHASE GOVERNMENT BONDS AND GIC'S THAT ARE GUARANTEED, BUT ARE YOU WILLING TO HAZARD A NEGATIVE REAL RETURN? IF NOT, YOU MUST SHOULDER SOME RISK. IN THE CURRENT ECONOMIC REALITY WE ARE OBLIGED TO TAKE ON MORE RISK IF WE EXPECT AN ACCEPTABLE RETURN. I SEE BTSX AS THE MOST PALATABLE OF THE ALTERNATIVES FOR CANADIAN INDIVIDUAL INVESTORS.

INVESTMENT BENCHMARKS (JULY 31, 2013, % CAGR)		
INDEX	10-YR.	5-YR.
MSCI WORLD	4.8	4.9
S&P 500 COMPOSITE	2.2	5.9
TSX COMPOSITE TR	8.3	1.3
TSX 60 INDEX TR	8.4	0.4
5-YR. GIC	2.5	1.9
CPI	1.8	1.2

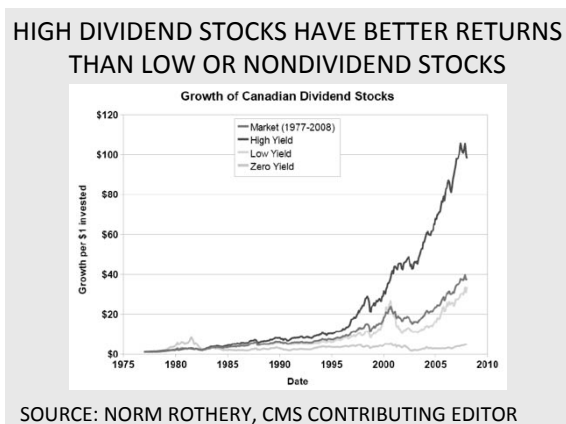
RECENTLY, THE U. S. HAS BEEN LEADING. WHY?

GIC'S HAVE THE LOWEST RETURNS SO WHY OWN THEM? THE PURPOSE OF FIXED-INCOME IN A PORTFOLIO IS CAPITAL PRESERVATION, NOT INCOME. FI IS LIKE A BOAT TRAILING ITS ANCHOR-IT GOES SLOWER, BUT IT IS SAFER IF THE BOAT GETS INTO SHALLOW WATER. FIXED-INCOME PREVENTS PORTFOLIO WRECKS AT THE EXPENSE OF LOWER RETURNS. SOME INVESTORS COUNT PENSIONS AS PART OF THEIR FIXED INCOME PORTFOLIO. UP TO YOU.

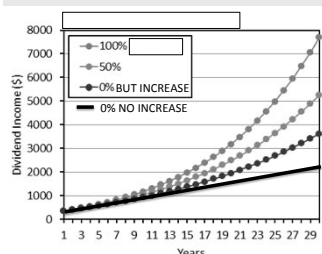
3-WHY INVEST IN BIG-CAP CANADIAN STOCKS?
 KEEP YOUR EYE ON TOTAL RETURNS, AFTER TAXES, INFLATION AND COSTS. THERE ARE 2 PARTS, CAPITAL GAINS AND DIVIDENDS. DIVIDENDS ACCOUNT FOR ≥50% OF THE TOTAL RETURNS. A DIVIDEND TAX CREDIT MEANS THEY ARE TAXED AT A LOWER RATE, SO FOR ONT. RESIDENTS IN THE TOP BRACKET, FOR EVERY 1\$ IN DIVIDENDS, \$1.28 MUST BE EARNED IN INTEREST FOR THE SAME RETURN.

DIVIDENDS ARE THE MOST EFFECTIVE WAY TO RECEIVE INVESTMENT INCOME. U. S. DIVIDENDS ARE NOT AS TAX EFFECTIVE. COMPANIES THAT DON'T PAY DIVIDENDS OFTEN BLOW THEIR EARNINGS ON STUPID DIVERSIFICATIONS, A DIVIDEND CAN KEEP THE STOCK PRICE FROM FALLING TOO FAR, AND A CHEQUE IN THE MAIL IS ALWAYS WELCOME. "A DIVIDEND IS A DICTATE OF MANAGEMENT. A CAPITAL GAIN IS A WHIM OF THE MARKET."

IN ORDER TO RECEIVE STRONG AND CONSISTENT DIVIDENDS FROM CANADIAN STOCKS ONE HAS TO CONSIDER THE 'BLUE-CHIP' COMPANIES THAT HAVE MANAGED TO INCREASE THEIR DIVIDEND PAYOUT YEAR-AFTER-YEAR FOR DECADES. THESE ARE HOUSEHOLD NAMES THAT EVERYONE RECOGNIZES. THESE ARE OUR SENIOR 'BLUE CHIPS' AND REPRESENTATIVE OF MOST SECTORS OF THE CANADIAN ECONOMY.



STOCK DIVIDENDS CAN BE COMPOUNDED BY REINVESTMENT. THIS OCCURS WHEN DIVIDENDS ARE CONVERTED TO MORE SHARES THAT ARE ADDED TO YOUR EXISTING SHARES.



DEPENDS ON THE INITIAL AMOUNT AND THE TIME AND FREQUENCY OF COMPOUNDING.

WHERE DO WE FIND HIGH YIELDING STOCKS?

HIGHEST YIELDING TSX COMPOSITE SECTORS (%)		
SECTOR	9/18/13	9/23/12
TELECOM	4.65	4.88
UTILITIES	4.88	4.79
REAL ESTATE I T ★	5.02	4.93
FINANCIAL	3.15	4.30
AVG.	4.43	4.73
TSX 60 INDEX	2.84	3.01
5-YR CDN BOND	2.10	1.38
CPI	1.30	1.78

HIGH YIELDING SECTORS ARE LEADING US OUT OF THE 'GREAT CONTRACTION'. TURF



TSXT vs. TSX – JUNE 30, 1999 TO JULY 19, 2013				
	TSXT		TSX	
30-JUN-99	14,756	30-JUN-99	7,010	
19-JUL-13	36,875	19-JUL-13	12,685	
% INCREASE	149.90	% INCREASE	80.96	
TOTAL RETURN BEATS THE INDEX BY 85.2%				

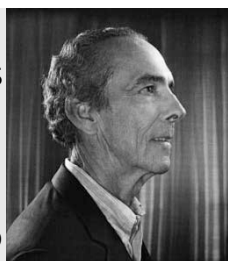
4-HOW CAN I INVEST IN DIVIDEND STOCKS?

CANADIAN DIVIDEND STOCKS — JULY 31, 2013		
CLASS	MER	10-YR. CAGR
MUTUAL FUNDS	2.2-2.4 %	6.6 %
ETF'S	0.30-0.60 %	~10.4 ???
TR INDEX	NON-INVESTABLE	10.7 %
BTSX	* (≤ 1 %)	12.9 %

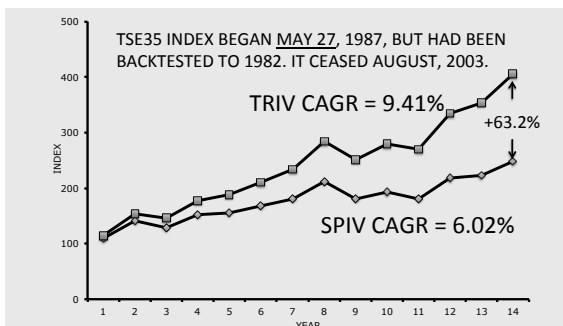
2 MAJOR CANADIAN INDEXES-TSX COMPOSITE & TSX 60. THE TSX 60 IS ~ TO THE DJ30 INDEX.

HISTORY OF BTSX

IN 1990 MICHAEL O'HIGGINS WROTE A BOOK CALLED "BEATING THE DOW". HIS 'DOGS OF THE DOW' USES AN EMOTION-FREE METHOD TO SELECT HIGH-DIVIDEND 'OUR FOUNDER' STOCKS. FROM 1974 TILL 2011 (37 YEARS) BTD HAS AVERAGED 14.84% VS. 9.74% FOR THE S&P 500 INDEX, AN INCREASE OF 52.4%.



WHEN I LOOKED AT THE STOCK PRICE AND TOTAL RETURN DATA FOR THE TSE35 (PRECURSOR OF THE TSX60) IN 1995 I WAS STRUCK BY HOW MUCH THE TOTAL RETURN INDEX WITH ITS REINVESTED DIVIDENDS HAD OUTPERFORMED SHARE PRICE APPRECIATION. I 'ADAPTED' THE STRUCTURED DECISION-MAKING PROCESS OF BTD TO THE TSE AND WROTE MY FIRST COLUMN IN 1996, THANKS TO THE ENCOURAGEMENT OF DALE ENNIS.



TSE35 INDEX 1982-1995. NOTE THE EFFECT OF COMPOUNDING. THIS WAS THE START OF BTSX.

5-HOW DOES 'BEATING THE TSX' WORK?

THE METHOD IS SIMPLE AND QUICK. A FEW MINUTES A YEAR CAN PICK A PORTFOLIO OF 10 STOCKS THAT USUALLY BEATS THE INDEX. DIVIDENDS ARE A HUGE DRIVING FORCE IN THE BLUE CHIP MARKET, AND LOWER PRICED STOCKS REGISTER HIGHER PERCENTAGE GAINS ON AVERAGE THAN HIGHER PRICED STOCKS. THUS, LOWER PRICED STOCKS WITH HIGHER YIELDS SHOULD OUTPERFORM AND THEY DO.

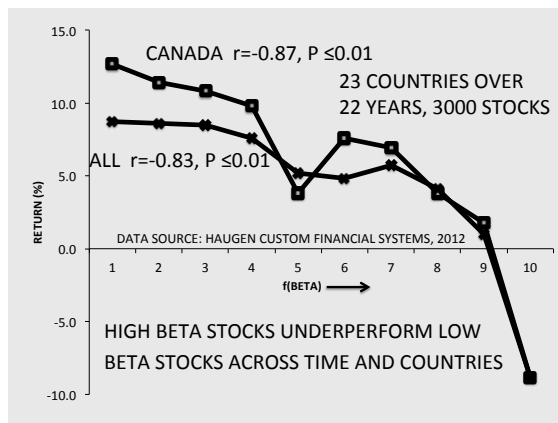
FIRST, GET A LISTING OF THE TSX60 INDEX STOCKS AND THEIR YIELDS FROM THE TMX WEBSITE, THE G&M, ETC. THEN RANK THE STOCKS FROM HIGH TO LOW BY YIELD. THROW AWAY ALL BUT THE TOP 10 YIELDERS, NOT COUNTING FORMER INCOME TRUSTS. THEN REARRANGE THE LIST WITH THE LOWEST PRICE AT THE TOP. THAT'S IT! NO COMPANY RESEARCH, PREDICTING EARNINGS, P/E RATIOS, ANIMAL SPIRITS, OR MARKET TIMING.

THE EASIEST APPROACH IS TO BUY EQUAL DOLLAR AMOUNTS OF THE 10 STOCKS WE'VE IDENTIFIED AND HOLD THEM FOR ONE YEAR AND REPEAT. \$1000 IS ABOUT THE LEAST YOU CAN ALLOT TO EACH PURCHASE. IF \$10,000 EXCEEDS YOUR COMFORT LEVEL YOU CAN BUY ONLY THE 5 LOWEST PRICED HIGH YIELDERS. THIS HAS THE ADVANTAGE OF LOWERING THE INITIAL COST TO \$5000 BEFORE COMMISSIONS BUT ALSO LIMITS DIVERSIFICATION.

MANY, ACTUALLY MOST, OF THE STOCKS THAT YOU HAVE SELECTED WILL HAVE DRIP AND SPP PLANS. COMPOUNDING IS THE MOST VALUABLE TOOL FOR INDIVIDUAL INVESTORS. SINCE IT IS LIKELY THAT SOME OF YOUR FIRST YEAR PICKS WILL ALSO BE ON THE SECOND YEAR'S LIST, KEEP THESE PLANS IN MIND. AN ADVANTAGE OF 'BEATING THE TSX' IS THAT THERE ARE RELATIVELY FEW SUBSTITUTIONS FROM YEAR TO YEAR, KEEPING COSTS LOW.

THE OBJECTIVE MECHANISM OF BTSX IS SIMPLE AND EASY. YEARLY RETURNS ARE IMPORTANT, BUT THE HEART OF THE BTSX METHOD IS AS FOLLOWS: **STOCKS MAY DROP OFF THE LIST BECAUSE THE PRICE HAS RISEN. KEEP THEM AS PART OF A GROWING PORTFOLIO OF BLUE-CHIP DIVIDEND STOCKS, MANY DRIPABLE, ACQUIRED AT A REASONABLE COST. LONG HOLDING TIMES ALLOW DIVIDENDS TO COMPOUND.**

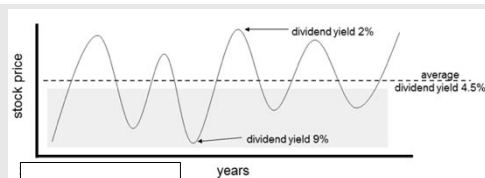
STOCKS ARE VOLATILE NOW SINCE THEY DO NOT TRADE ON FUNDAMENTALS BUT ON EMOTION AND NEWS. HIGH DIVIDEND STOCKS SHOW LOWER VOLATILITY BECAUSE THEY HAVE MORE PREDICTABLE CASH FLOWS AND STABLE EARNINGS. β IS A MEASURE OF A STOCK'S VOLATILITY (S.D.) IN RELATION TO THE MARKET. HIGH β STOCKS ARE MORE VOLATILE THAN THE INDEX; LOW β STOCKS ARE LESS VOLATILE. BLUE-CHIP STOCKS USUALLY HAVE A LOWER β .



WHY DOES BTSX WORK?

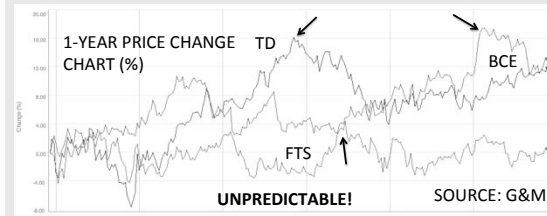
1. STOCK PRICE AND YIELD ARE INVERSELY RELATED IF THE DIVIDEND IS CONSTANT.

$$\text{DIVIDEND YIELD} = \frac{\text{ANNUAL DIVIDEND PER SHARE}}{\text{STOCK PRICE PER SHARE}}$$



IT IS ONLY A GOOD INVESTMENT IF YOU DIDN'T PAY TOO MUCH!

2. EVEN LOW BETA BLUE-CHIP STOCKS EXHIBIT SIGNIFICANT CYCLICALITY OVER TIME.

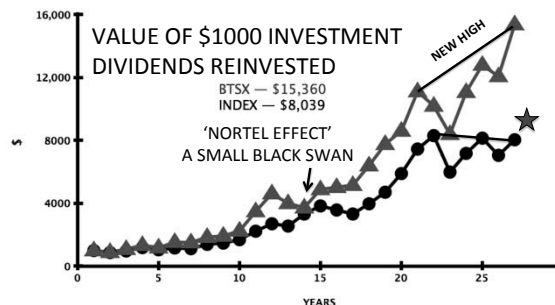


SELECT STOCKS WHEN YIELD IS HIGH AND PRICE IS LOW. HOW? WE ARE SIMPLY EFFICIENTLY EXPLOITING SMALL BUT FAVOURABLE VALUATION SHIFTS IN LOW β STOCKS.

6-HOW HAS BTSX PERFORMED?

BEATING THE TSX – 26 YEAR RESULTS (1987-2013)		
	AVG. RETURN (%)	\$1K INVEST
BTSX	12.56	\$15,360
TR INDEX	9.52	\$8,039
% INCR. VS. INDEX	+31.9	+91.1

A 32% INCREASE IN RETURN IS HUGE. BTSX HAS TROUNCED ALL COMPARABLE MUTUAL FUNDS & ETFs, BEAT THE INDEX 73% OF THE TIME FOR THE PAST 26 YR., 83% FOR THE PAST 6 YR.



91% ADVANTAGE FOR BTSX. WE ARE GETTING CLOSE TO DOUBLING THE INDEX RETURN.

STOCK	SYM	OPEN	FINAL	YIELD (%)	CHANGE (%)
Manulife	MFC*	\$11.23	\$15.96	4.63	42.07
TransAlta	TA*	\$17.37	\$15.29	6.68	-11.97
Shaw Comm.	SJR.B	\$19.52	\$23.64	4.71	21.11
Sun Life	SLF*	\$21.55	\$30.24	6.68	40.32
Husky Energy	HSE	\$23.30	\$30.53	5.15	31.03
Power Corp.	POW	\$23.43	\$28.66	4.95	22.30
Thomson Reuters	TRI	\$28.70	\$36.37	4.46	26.72
BCE Inc.	BCE*	\$40.46	\$47.92	5.36	18.44
Bank of Montreal	BMO*	\$54.50	\$63.21	5.14	15.98
CIBC	CM*	\$70.03	\$80.13	5.14	14.41
TSX60 TR (%)		14.02	AVG.	5.29	22.04
BTSX (%)		94.86	TOTAL		27.32

FINAL RESULTS FOR THE 2012-13 PORTFOLIO AS OF MAY 24TH

*= DRIP & SPP PLANS; AVG. TSX60 YIELD = 3.02%

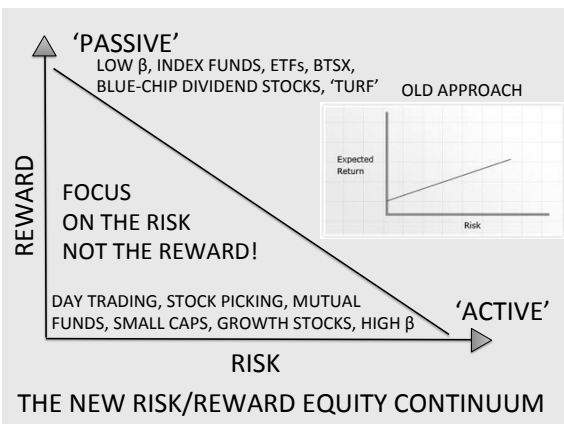
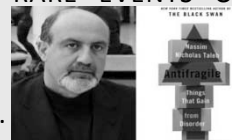
NOTE THAT THE TSX 60 SPIV INDEX ONLY GAINED ~11% YOY

2013-14 BTSX PORTFOLIO, MAY 24, 2013 (β, YEAR FOUNDED)	YIELD (%)
lamgold Corp. IMG (0.630, 1991)	4.91
†TransAlta TA* (0.147, 1911)	7.59
Barrick Gold Corp ABX (0.525, 1983)	4.18*
†Shaw Comm. SJR.B (0.287, 1966)	4.31
Sun Life SLF* (1.076 1865)	4.76
†BCE Inc. BCE* (0.020, 1880)	4.86
Bank of Nova Scotia BNS* (0.641, 1832)	4.04
†Bank of Montreal BMO* (0.621, 1817)	4.68
National Bank NA* (0.704, 1859)	4.31
†CIBC CM* (0.715, 1867) AVG. β=0.537, AGE=116 YR.	4.69
AVG. (NO EX-INCOME TRUSTS OR REITS. *=DRIP & SPP PLANS)	4.84
Government of Canada 10-yr. benchmark bond	1.95

7-WHAT IS THE DOWNSIDE RISK?

IT IS ALWAYS IMPORTANT FOR INVESTORS TO THINK ABOUT RISK, BUT PARTICULARLY NOW IN LIGHT OF THE 'NEW NORMAL' CONDITIONS. THE 'NEW NORMAL' DESCRIBED BY BILL GROSS AT PIMCO TRANSLATES TO LOWER RETURNS, HIGHER INFLATION, HIGHER TAXES, MORE VOLATILITY, AND IRRATIONAL MARKETS FOR INVESTORS. THIS IS A STRUCTURAL, NOT A CYCLICAL CHANGE AND MEANS MORE RISK.

WE MAKE MISTAKES BY THINKING ABOUT THE POTENTIAL RETURN OF AN INVESTMENT. WE SHOULD VIEW OUR INVESTMENTS WITH THE IDEA OF THEM SURVIVING RELATIVELY UNSCATHED IF A BAD BLACK SWAN OCCURS. BLACK SWANS ARE LARGE-SCALE, UNPREDICTABLE, AND RARE EVENTS OF MASSIVE CONSEQUENCE. READ TALEB'S BOOK 'ANTIFRAGILE' FOR MORE.



OVER A 5-YR. PERIOD, ONLY ~10%, OF ACTIVELY MANAGED CANADIAN EQUITY FUNDS OUTPERFORMED THE TSX COMPOSITE (SPIVA, 2012). % OF FUNDS SURVIVING OVER 5 YR. ~69%. CAN'T BEAT THE INDEX OVER THE LONG HAUL. MER'S (AVG.=2.36%) WILL KILL YOU! BTSX—YOU CAN IGNORE ALL STOCK-PICKING TOOLS, e. g., TECHNICAL ANALYSIS, MARKET TIMING, MOMENTUM, COSTLY RESEARCH, ETC. STICK WITH PASSIVE INVESTING.

RISKS SPECIFIC TO BTSX

- *PRICES MAY DIP IF BOND YIELDS INCREASE
- *BTSX PORTFOLIOS ARE TYPICALLY OVERWEIGHTED IN FINANCIALS, UTILITIES, AND TELCOS, THUS ARE INTEREST SENSITIVE
- *YOU HAVE NO ONE TO BLAME BUT YOURSELF
- *TAXES ON DIVIDENDS MAY/WILL INCREASE
- *INDEX ITSELF — LAIDLAW (-94%) 1999, NT
- *DIVIDEND MAY NOT INCREASE, OR BE CUT MFC
- *USER ERROR-NOT STAYING THE COURSE

8-CONCLUSIONS

OVER 16 YR. NOT MUCH HAS CHANGED. BTSX CONTINUES TO BE A LOW-RISK, PASSIVE WAY TO BEAT THE INDEX, IMPOSE DISCIPLINE AND PATIENCE, AND LOWER INVESTING COSTS. IT IS SIMPLE TO EXECUTE, EASY TO UNDERSTAND AND REQUIRES LITTLE TIME TO USE. BTSX PROMOTES DIVIDEND COMPOUNDING AND RESULTS IN A PORTFOLIO OF DIVIDEND-PAYING STOCKS OBTAINED AT A REASONABLE COST.

YOU CAN EMPOWER YOURSELF AS AN INDIVIDUAL INVESTOR. KNOWLEDGE IS EMPOWERMENT. EDUCATE YOURSELF. USE THE CMS AND SHARECLUBS. LIVE SIMPLY. WATCH YOUR COSTS. SAVE. IGNORE BOTH THE PROPHETS OF APOCALYPSE AND THE CHEERLEADERS OF RAPTURE. COURAGE AND PATIENCE ARE THE MOST IMPORTANT ATTRIBUTES OF SUCCESSFUL INDIVIDUAL INVESTORS! THANKS FOR COMING!