

BEATING THE TSX – IT WORKS!
(OR, BUILDING A DIVIDEND PORTFOLIO)

TORONTO CMS CONFERENCE

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OUTLINE

- ❖ ASSET ALLOCATION
- ❖ ACTIVE VS. PASSIVE INVESTING
- ❖ WHY DIVIDEND STOCKS
- ❖ SELECTING DIVIDEND STOCKS
- ❖ 'BEATING THE TSX'
- ❖ SUMMARY AND CONCLUSIONS
- ❖ QUESTIONS



STEP 1 — A PLAN, THEN ASSET ALLOCATION

- ❖ REGISTERED/NONREGISTERED
USUALLY BEST TO MAX THE REGISTERED PLANS (TFSA, RRSP, ETC.), BUT YOU LOSE DIVIDEND TAX CREDIT & DRIP PLANS
- ❖ FIXED INCOME/EQUITIES REF.
FIXED INCOME IS TOUGH NOW & ALWAYS FOR DIY INVESTORS — BONDS, ETFs, GICs, CSBs*. 75/25, 50/50, 25/75? RISK TOLERANCE?

WHAT'S WRONG WITH GICs?

FIXED INCOME INVESTMENTS SHOULD PRESERVE CAPITAL		
INVESTMENT	5-YR. AVG.	REAL RETURN
CDN EQUITY FUNDS	-2.1	-4.1
AVG. MER	+2.4	
TSX TOTAL RETURN	+0.2	-1.8
5-YR. GIC	+2.2	+0.2

DATA SOURCE-G&M GLOBEFUND, CPI ~ 2.0, AS OF 10/12/12

IF THE NEXT 5 YEARS ARE LIKE THE LAST 5 YEARS...
CURRENT POSTED 5-YR. GUARANTEED GIC RATES
~ 2.5-2.8%. YOU HAVE TO SHOP AROUND.

INVESTMENT RISKS

- ❖ GOVERNMENT BONDS — NEGATIVE REAL RETURNS, REPLACEMENT RISK, INFLATION
- ❖ CORPORATE BONDS — BANKRUPTCY (LOSS OF CAPITAL), EARLY REDEMPTION
- ❖ BLUE-CHIP HIGH DIVIDEND STOCKS — CUTTING DIVIDENDS (e.g., MFC), INCREASED TAXES ON DIVIDENDS, STAGNANT ECONOMY
- ❖ 'COLLECTABLES' — NO MARKET

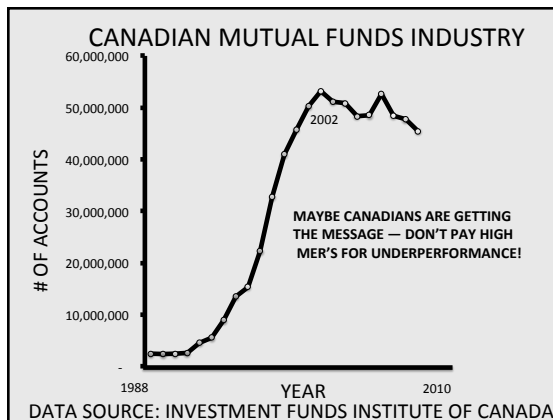
❖ GEOGRAPHIC ALLOCATION

DEPENDS IN PART ON WHERE YOU ARE GOING TO SPEND IT, USUALLY CANADA.

❖ SECTOR ALLOCATION

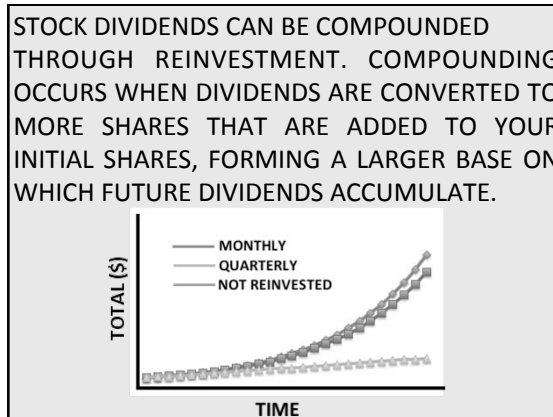
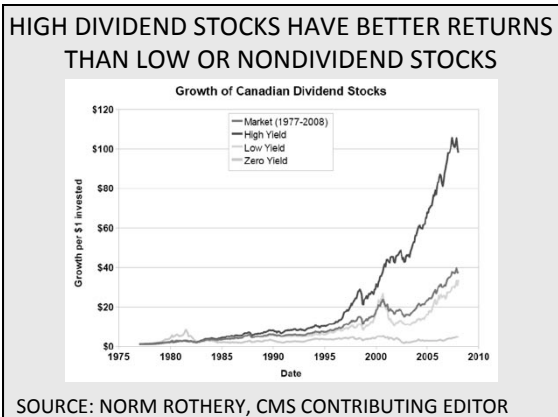
FOR ME, THIS IS DICTATED BY DIVIDENDS. WHY DIVIDENDS? DIVIDENDS ACCOUNT FOR THE MAJORITY OF TOTAL RETURNS OVER THE LONG TERM. ALSO A TAX BREAK. 5% CANADIAN DIVIDEND = AFTER-TAX INTEREST EQUIVALENT OF 6.41% (IN ONTARIO @ \$65K, 2011).

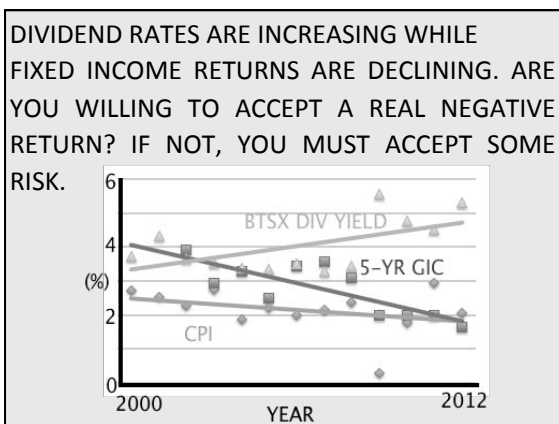
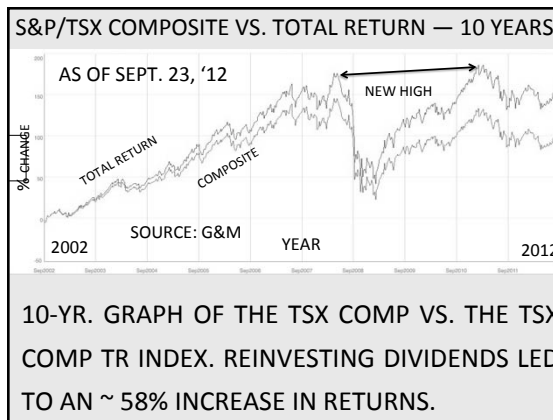
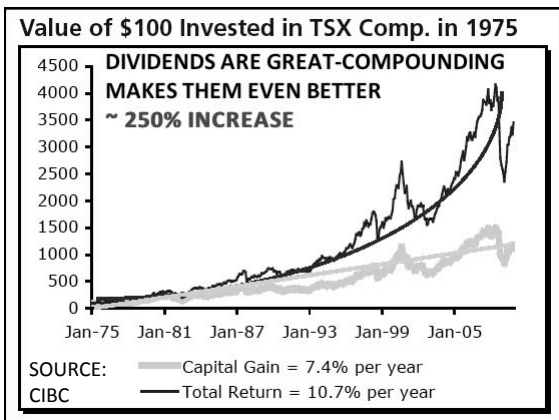
STEP 2 — ACTIVE VS. PASSIVE INVESTING
 CDN. EQUITY FUNDS BEATING THE INDEX OVER 5 YR. = 2.74% (DO YOU LIKE THOSE ODDS?)
 FUNDS 5 YR. RETURN = -1.41% (MER=2.42%)
 INDEX 5 YR. RETURN = +1.30%
 BTSX 5 YR. RETURN = +3.20%
 % OF FUNDS SURVIVING OVER 5 YR. = 68.5%
 THE DEBATE IS OVER! CAN'T BEAT THE INDEX OVER A LONG PERIOD OF TIME. MER'S WILL KILL YOU. S&P/TSX TR INDEX NON-INVESTABLE.
 SOURCE: SPIVA* (AS OF 2011)



STEP 3 — CONCENTRATE ON DIVIDEND STOCKS
 DIVIDENDS ARE A SHARE OF A COMPANY'S PROFITS THAT IT PAYS TO ITS INVESTORS. DIVIDENDS + CAPITAL GAINS FORM THE TOTAL RETURN FROM AN INVESTMENT IN A PUBLIC COMPANY. DIVIDENDS ARE MORE IMPORTANT THAN MOST INVESTORS REALIZE. DIVIDENDS HAVE ACCOUNTED FOR >60% OF THE S&P/TSX TOTAL RETURNS OVER THE LONG HAUL.

- SUPERIOR DIVIDEND COMPANIES HAVE SEVERAL COMMON ATTRIBUTES:
1. LARGE AND MATURE COMPANIES;
 2. THEY ARE PAST THEIR GROWTH PHASE WITH NO MAJOR EXPENDITURES;
 3. THEY HAVE GOOD MANAGEMENT WITH SOLID CORPORATE GOVERNANCE;
 4. THEY HAVE STRONG CASH FLOW AND EARNINGS GROWTH. 'BLUE-CHIPS'.





WHAT ABOUT 'DIVIDEND ACHIEVERS' FUNDS?

MORNINGSTAR: "IN BAD TIMES, YIELD-WEIGHTED FUNDS PILE INTO DISTRESSED FIRMS WITH UNSUSTAINABLY HIGH DIVIDENDS. A HIGH YIELD OFTEN MEANS DIVIDEND CUTS OR SLOW/NEGATIVE EARNINGS GROWTH. DESPITE SCREENING FOR COMPANIES THAT HAVE INCREASED THEIR DIVIDENDS EVERY YEAR FOR AT LEAST 5 YEARS, THESE FUNDS FELL HARD WHEN THE FINANCIAL CRISIS ERUPTED. 5 YEARS OF GROWTH DOESN'T MEAN DURABILITY."

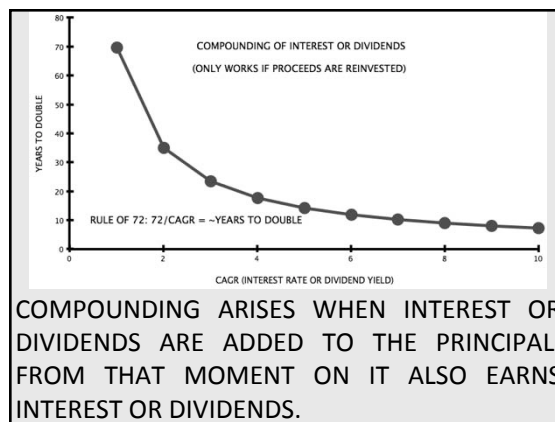
WHAT ABOUT GLOBAL DIVIDENDS?

FOREIGN DIVIDENDS DO NOT QUALIFY FOR THE DIVIDEND TAX CREDIT AND ARE FULLY TAXABLE. THERE IS A 15% WITHHOLDING TAX ON FOREIGN DIVIDENDS. TO AVOID DOUBLE TAXATION, CANADA ALLOWS A FOREIGN TAX CREDIT. ALSO, I AM A LITTLE LEERY OF INVESTING IN OTHER COUNTRIES AT THIS TIME BECAUSE OF FINANCIAL PROBLEMS. STOCK FUNDAMENTALS HAVE OFTEN GONE OUT THE WINDOW, REPLACED WITH FEAR AND GREED.

WE HAVE A FINE ARRAY OF DIVIDEND PAYERS HERE, BUT IF, FOR DIVERSIFICATION, I WANT TO OWN A BIG PHARMA I MUST GO TO THE U. S., THE SAME WITH A BIG TOBACCO COMPANY, A BIG FOOD COMPANY, A BIG CONSUMER PRODUCTS COMPANY, ETC. THAT IS WHY I OWN JNJ, PM, KFT*, PG, ETC. IN THE STATES AND TAKE MY LUMPS WITH THE LACK OF A DIVIDEND TAX CREDIT. THESE COMPANIES HAVE INTERNATIONAL SALES AND DRIP PLANS.

COMPOUNDING IS THE MOST VALUABLE TOOL INDIVIDUAL INVESTORS HAVE TO WORK WITH. THE COMPOUNDING EFFECT DEPENDS ON:

1. THE AMOUNT TO BE COMPOUNDED-THUS, NEED HIGH & SUSTAINABLE DIVIDENDS;
2. THE TIME OVER WHICH THE DIVIDENDS ARE COMPOUNDED-THUS, THE LONGER THE BETTER, i. e., BUY-AND-HOLD;
3. THE FREQUENCY WITH WHICH DIVIDENDS ARE PAID-MONTHLY IS BETTER THAN QUARTERLY, IS BETTER THAN YEARLY.



COMPOUNDING ARISES WHEN INTEREST OR DIVIDENDS ARE ADDED TO THE PRINCIPAL. FROM THAT MOMENT ON IT ALSO EARNS INTEREST OR DIVIDENDS.

HOW CAN I REINVEST MY DIVIDENDS TO TAKE ADVANTAGE OF COMPOUNDING? (REF.)
 A CANADIAN DRIP (DIVIDEND REINVESTMENT PLAN) IS AN INVESTMENT OPTION OFFERED DIRECTLY FROM THE UNDERLYING COMPANY. YOU DON'T RECEIVE THE DIVIDEND DIRECTLY AS CASH; INSTEAD ALL IS INVESTED INTO NEW EQUITY SHARES AT NO COMMISSION. YOU MUST STILL PAY TAX ON THE DIVIDEND WHETHER IT IS RECEIVED OR REINVESTED.

THIS ALLOWS THE INVESTMENT RETURN FROM DIVIDENDS TO BE IMMEDIATELY INVESTED FOR THE PURPOSE OF PRICE APPRECIATION AND COMPOUNDING, WITHOUT INCURRING BROKERAGE FEES OR WAITING TO ACCUMULATE ENOUGH CASH FOR A FULL SHARE OF STOCK. DRIPS, BY THEIR NATURE, ENCOURAGE LONG-TERM INVESTMENT. MANY COMPANIES OFFER A SHARE PURCHASE PLAN (SPP) THAT ALLOWS INVESTORS TO MAKE OPTIONAL CASH PURCHASES OF STOCK SHARES.

DO NOT CONFUSE THESE DRIPS W/ SYNTHETIC BROKERAGE DRIPS. SYNTHETICS OFFER:

- ❖ WHOLE SHARE PURCHASES ONLY, NO FRACTIONAL SHARES.
- ❖ MAY OR MAY NOT PASS ALONG TO YOU ANY DRIP DISCOUNT. DO NOT OFFER SPP PLANS.
- ❖ MAY OR MAY NOT WORK FOR ALL COMPANIES YOU OWN, BUT THEY ARE RRSP/RESP/TFSA COMPATIBLE.
- ❖ THEY ARE BETTER THAN NOTHING.

WHERE DO WE FIND HIGH YIELDING STOCKS?

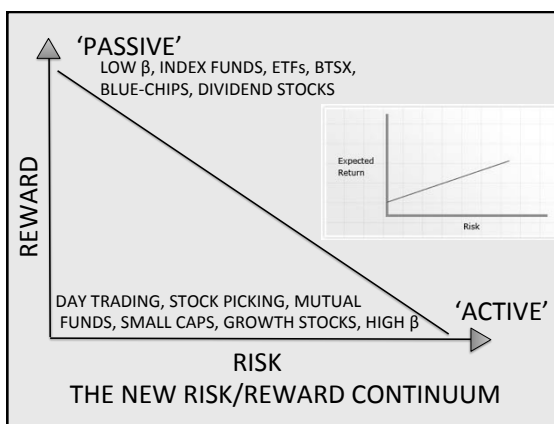
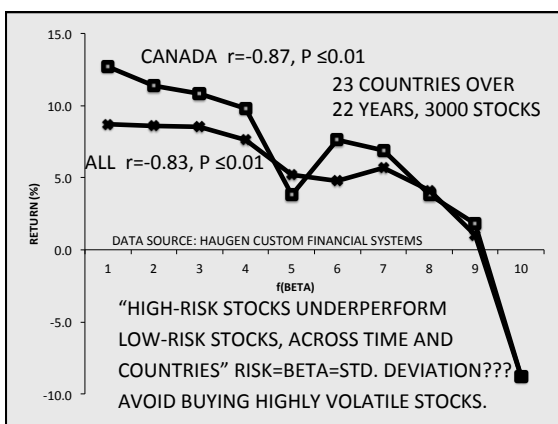
HIGHEST YIELDING TSX COMPOSITE SECTORS (9/23/12)		
SECTOR	YIELD (%)	3-YR SPIV (%)
TELECOM	4.88	41.9
UTILITIES	4.79	26.4
REAL ESTATE I T	4.93	57.8
FINANCIAL	4.30	2.0
AVG.	4.73	32.0
TSX 60 INDEX	3.01	5.3
5-YR CDN BOND	1.38	
CPI	1.78	

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

Canadian 16 Largest Capitalized Companies as of Sept. 23, 2012 — 'SWEET SIXTEEN'				
SYM	Company	Market Cap (x10 ³)	Yield (%)	β
RY**	Royal Bank of Canada	80.87	4.23	0.892
TD**	Toronto-Dominion Bank	74.72	3.76	0.826
BNS*	Bank of Nova Scotia	63.72	4.26	0.873
SU*	Suncor Energy Inc.	50.74	1.57	1.780
ABX	Barrick Gold Corp.	41.64	1.89	0.643
IMO*	Imperial Oil Ltd.	38.98	1.04	0.980
BMO*	Bank of Montreal	37.51	4.94	0.841
CNR	Cdn. National Railway	37.27	1.74	0.438
G	Goldcorp	37.09	1.16	0.853
POT	Potash Corp.	36.85	1.91	6.285
CNQ	Cdn. Natural Resources	35.30	1.31	2.272
BCC*	BCE	33.02	5.27	0.158
TRP*	TransCanada Corp	31.60	3.91	0.242
CM*	Cdn. Imperial Bank	31.33	4.84	0.884
ENB*	Enbridge	30.44	2.96	0.368
HSE	Husky Energy Inc.	26.14	4.45	1.159
		AVG.(16)	r = -0.36	1.218
		AVG.(8)	4.27	0.636

FINANCIAL-5, MATERIALS-4, ENERGY-3, UTILITY-2, TELECOM-1, INDUSTRIALS-1, REAL ESTATE-0, * = DRIP + SPP, ** = DRIP

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 .



SO THEN, WHERE DO WE FIND CANADIAN HIGH-DIVIDEND STOCKS? IN A BLUE-CHIP INDEX. FOR US THAT IS THE S&P/TSX 60 INDEX, A MARKET-CAP WEIGHTED INDEX OF CANADA'S LARGEST STOCKS. IN COMPARISON, MOST SMALL- AND MID-CAP STOCKS SPEND MOST OF THEIR EARNINGS TO REINVEST BACK INTO THE BUSINESS, THUS PAYING LITTLE OR NO DIVIDENDS TO SHAREHOLDERS.

STEP 4 — SELECTING DIVIDEND STOCKS

NOTE THAT WE ARE ¼ OF THE WAY THROUGH THE PORTFOLIO BUILDING PROCESS BEFORE WE EVEN BEGIN TO CONSIDER INDIVIDUAL STOCKS. NOTE ALSO THAT WE CAN JUST SKIP THE SELECTION STEP AND BUY ETFs OR FUNDS, BUT YOUR RETURNS WILL SUFFER DUE TO COSTS. KEEP YOUR INVESTING COSTS LOW, ESPECIALLY IN LIGHT OF THE 'NEW NORMAL'.

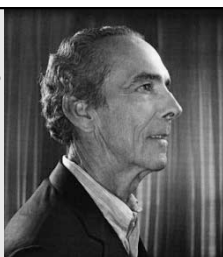
6-YEAR COMPARISON OF XDV (ETF, MER=0.5%) VS. BTSX				
YEAR	XDV	INDEX	BTSX	INDEX
2011	3.49	4.09	-5.60	-13.40
2010	12.82	13.32	15.63	13.49
2009	36.9	37.83	31.89	19.84
2008	-30.84	-30.80	-17.71	-27.90
2007	-0.77	-0.41	-8.21	11.47
2006	15.53	16.07	29.14	26.37
AVG.	6.19	6.68	7.52	4.98
% INC. VS. INDEX	-7.41%		51.12%	
XDV VS. BTSX			+21.5%	TSX=3.21%

STEP 5— BEATING THE TSX

BTSX IS A SIMPLE OBJECTIVE METHOD FOR BUILDING A PORTFOLIO OF BLUE-CHIP, HIGH-YIELDING STOCKS AT A REASONABLE PRICE. BTSX IS EASY TO IMPLEMENT AND NEEDS NO SPECIAL MATHEMATICAL SKILLS. OVER THE PAST 25 YEARS IT HAS BEAT A CANADIAN LARGE-CAP TR INDEX BY AN AVERAGE OF 28%. IT IMPOSES DISCIPLINE AND PATIENCE, AND ELIMINATES MANAGEMENT FEES.

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 NOW (37 YEARS) BTM 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 IN 1995 I WAS STRUCK BY HOW MUCH THE TOTAL RETURN INDEX WITH ITS REINVESTED DIVIDENDS HAD OUTPERFORMED STOCK PRICE APPRECIATION. I ADOPTED THE STRUCTURED DECISION-MAKING PROCESS OF BTM TO THE TSE AND WROTE MY FIRST 'BEATING THE TSE' COLUMN IN 1996, THANKS TO THE ENCOURAGEMENT OF DALE ENNIS.

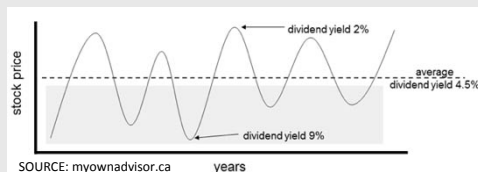
HOW DOES BTSX WORK? (REF.)

THE LIST OF S&P/TSX 60 STOCKS IS ORDERED FROM HIGH TO LOW BY DIVIDEND YIELD, THE TOP 10 STOCKS ARE THEN ORDERED FROM LOW TO HIGH PRICE. THE TOP 10 STOCKS ARE PURCHASED IN EQUAL DOLLAR AMOUNTS AND HELD FOR ONE YEAR. INVESTORS BUILD UP A PORTFOLIO OF HIGH QUALITY STOCKS PURCHASED AT A REASONABLE COST. NO HOCUS POCUS, ANIMAL SPIRITS, CHARTS, ETC.

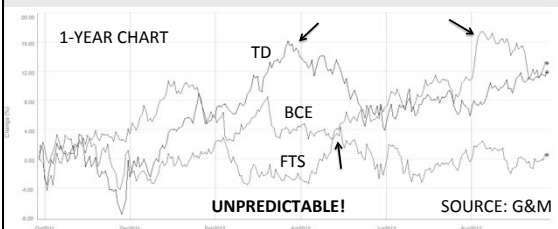
WHY DOES BTSX WORK?

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

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



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

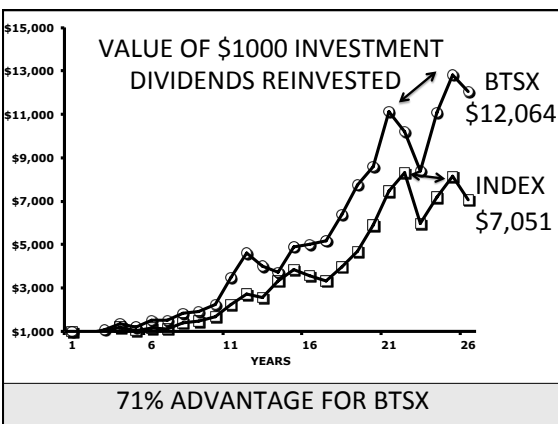


SELECT STOCKS WHEN YIELD IS HIGH AND PRICE IS LOW. HOW? PICK STOCKS WITH HIGH YIELDS ON A GIVEN START DATE & REPEAT YEARLY.

HOW HAS BTSX PERFORMED?

BEATING THE TSX – 25 YEAR RESULTS (1987-2011)		
	AVG. RETURN (%)	\$1K INVEST
BTSX	11.97	\$12,064
TR INDEX	9.34	\$7,051
% INCR. VS. INDEX	+28.1	+71.1

A 28% INCREASE IN RETURN IS HUGE. BTSX HAS BEATEN ALL COMPARABLE MUTUAL FUNDS & ETFs, BEAT THE INDEX 64% OF THE TIME FOR THE PAST 25 YR., 80% FOR THE PAST 5 YR.



BEATING THE TSX — ‘REAL’ RETURNS

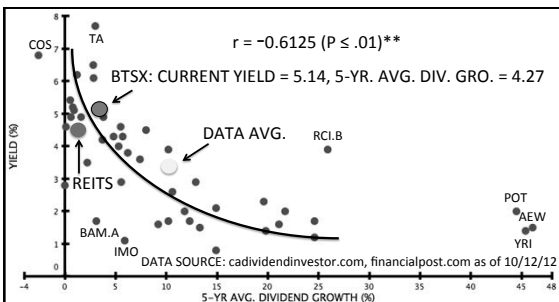
25-YEAR RETURNS, \$1000 INVESTMENT, CPI = 2.29%				
	VALUE	CAGR (%)	‘REAL’ (%)	VALUE
BTSX	\$12,064	10.47	8.18	\$7,140
TR INDEX	\$ 7,051	8.13	5.84	\$4,133
5-YR. GIC	\$ 4,243	5.95	3.66	\$2,456
BTSX/GIC	\$ 8,154	8.21	5.92	\$4,298

EVEN A CAUTIOUS INVESTOR WHO USED A 50/50 SPLIT BETWEEN BTSX AND 5-YR. GIC’S WOULD HAVE BEATEN THE INDEX AFTER CPI.

IF I CAN GET THESE RETURNS FOR 10-15 YEARS I WILL DO BETTER THAN ~ 95% OF MY PEERS.

GET RICH SLOWLY!
 * = DRIP & SPP
 † = ‘SWEET 16’
 AVG. 5 YR. DIV. GRO. = 4.27%
 OUR TRUMP CARD

COMPANY (AS OF 9/23/12)	YIELD (%)
TransAlta Corp. TA-T* (1911)	7.84
Sun Life Financial Inc. SLF-T* (1865)	6.10
†BCE Inc. BCE-T* (1880)	5.27
†Bank of Montreal BMO-T* (1817)	4.94
†CIBC CM-T* (1867)	4.84
Power Corp of Canada POW-T (1925)	4.72
Shaw Communications SJR.B-T (1966)	4.56
†Husky Energy HSE-T (1938)	4.45
Manulife Financial Inc. MFC-T* (1887)	4.38
Thomson Reuters TRI-T (1931) AVG.=113 YR	4.32
AVG. (NO EX-INCOME TRUSTS OR REITS)	5.14
TSX 60 INDEX	3.01



DIVIDEND YIELD OR DIVIDEND GROWTH?
 DATA FROM 45 S&P/TSX 60 STOCKS + REITS
 FOCUS ON YIELD RATHER THAN DIV. GROWTH

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 MEANS WE WILL ALL HAVE TO WORK LONGER, SAVE MORE, AND SPEND LESS. THIS IS A STRUCTURAL, NOT A CYCLICAL CHANGE. IF KEYNESIAN QUANTITATIVE EASING/ FINANCIAL STIMULUS WORKS, WHY DO WE KEEP NEEDING MORE? QE $\rightarrow \infty$? \$40B/MO?

THE OBJECTIVE MECHANISM OF BTSX IS SIMPLE AND EASY. STOCKS OFTEN STAY ON THE LIST FOR SEVERAL YEARS, MEANING LOW TURNOVER AND TRADING COSTS. USUALLY STOCKS DROP OFF THE LIST BECAUSE THE PRICE HAS RISEN. YOU CAN KEEP THEM AS PART OF A GROWING PORTFOLIO OF BLUE-CHIP DIVIDEND STOCKS, MANY HAVING DRIP PLANS, ACQUIRED AT A REASONABLE COST. LONG HOLDING TIMES ALLOW DIVIDENDS TO COMPOUND.

IN ORDER TO SUCCEED AT DIVIDEND INVESTING INDIVIDUALS NEED TO:

1. CREATE A PORTFOLIO OF CANADIAN BLUE-CHIP DIVIDEND STOCKS PURCHASED AT A REASONABLE PRICE;
2. EMPLOY A BUY-AND-HOLD STRATEGY;
3. REINVEST DIVIDENDS TO FOSTER THE COMPOUNDING EFFECT.

WHILE THE PRINCIPLES ARE EASY, THEIR IMPLEMENTATION CAN BE DIFFICULT IN TIMES SUCH AS WE ARE NOW EXPERIENCING.

ADVANTAGES OF THE BTSX SYSTEM:

- ❖ NO BROKER OR FINANCIAL ADVISOR
- ❖ NO MUTUAL FUNDS OR MANAGEMENT FEES
- ❖ NO TIME CONSUMING RESEARCH
- ❖ LOW-RISK, LESS STRESS, INDEPENDENCE

DISADVANTAGES OF THE BTSX SYSTEM:

- ❖ NO ONE TO BLAME BUT YOURSELF
- ❖ DIVIDEND CUTS, TAX CODE CHANGES
- ❖ INDEX ITSELF — LAIDLAW (-94%) 1999

SHARECLUBS

SHARECLUBS ARE INFORMAL GEOGRAPHIC GROUPS OF THOSE WHO ARE INTERESTED IN SHARING THEIR INVESTMENT KNOWLEDGE.

- ❖ BEGAN IN 1997, ORGANIZED THROUGH THE EFFORTS OF THE CMS AND DALE ENNIS;
- ❖ NOT AN INVESTMENT CLUB, WE LOOK AFTER OUR OWN FINANCIAL DECISIONS.
- ❖ THE GOAL IS TO EMPOWER MEMBERS TO TAKE CONTROL OF THEIR INVESTMENTS.
- ❖ 25 ONTARIO CLUBS, OTHERS IN THE WEST.

SHARECLUBBERS SHARE OUR MISTAKES AND SUCCESSES, AND LEARN FROM OTHERS. THERE ARE NO FEES, BUT MEMBERS ARE STRONGLY ENCOURAGED TO SUBSCRIBE TO THE CMS.



STEP 6—CONCLUSIONS YOU CAN EMPOWER YOURSELF AS AN INDIVIDUAL INVESTOR. KNOWLEDGE IS EMPOWERMENT. USE THE CMS AND SHARECLUBS. LIVE SIMPLY. 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!