

# Disciplined Alpha Dividend Strategy

Portfolio and Economic Commentary – 1<sup>st</sup> Quarter 2017





**DISCIPLINED ALPHA DIVIDEND STRATEGY COMMENTARY**

As value investors, we constantly focus on our duty to protect the principal of our investments even as we look for ways to grow them over time as well. As economists, we remain alert to trends taking place in the larger global economy. As analysts, we seek to invest in securities priced with a margin of safety in order to account for their near term volatility and our uncertainty about what the future holds. With this in mind, we look for opportunities in three specific categories: classic value, persistent earners, and distressed or contrarian.

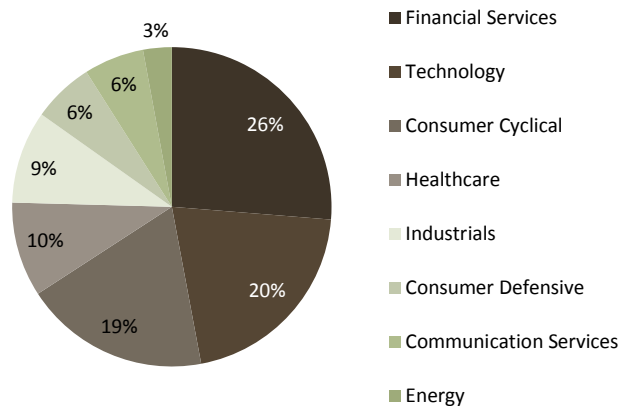
Classic value stocks sell at attractive valuations and provide above-average dividend yields and growth. Persistent earners are companies which have steady and predictable earnings and that are selling below their historic valuation. The distressed/contrarian category refers to stocks that are out of favor due to what we perceive to be temporary factors and are likely to appreciate substantially as the temporarily distressing factor recedes. Typically the distressed category is the smallest in the portfolio.

**PERFORMANCE COMMENTARY**

The Disciplined Alpha Dividend strategy gained 2.14% while the Russell 1000 Value index returned 3.27% for the quarter. The strategy has produced outstanding ten-year risk adjusted returns roundly besting its indices and peer group for the period earning a Morningstar 4-star overall rating. The trailing annualized ten year returns were 8.06% for the strategy, 5.93% for the Russell 1000 Value index and 6.89% for the Dow Jones US Select Dividend index.

Though the strategy produced sound absolute returns, our stock selection had a negative effect on relative performance. Our sector allocation weighting also slightly detracted from relative performance leading to a negative active return against the Russell 1000 Value index for the quarter. The technology, consumer defensive and financial services sectors were our largest contributors to relative outperformance, while the industrials, consumer cyclicals and energy sectors were the largest detractors. Though maintaining a focus on dividends and above average income generation, we believe the utility and real estate sectors remain overvalued and will perform poorly in a potentially rising interest rate environment. The top performers for the quarter were Apple (24.6%), Philip Morris (24.5%), KKR & Co. (19.5%), Cisco Systems (12.8%) and Principal Financial Group (9.9%). The bottom performers were Pitney Bowes (-12.5%), New York Community Bancorp (-11.2%), Occidental Petroleum (-10.0%), Marathon Oil (-8.4%) and Exxon Mobil (-8.3).

**Sector Allocation (Morningstar)**



**Top Ten Holdings**

**Weight**

Apple Inc	3.77%
Principal Financial	3.52%
JPMorgan Chase & Co.	3.40%
Qualcomm Inc	3.39%
Cisco Systems Inc	3.39%
International Business Machines	3.37%
Microsoft Corp	3.34%
Hanesbrands Inc	3.31%
MetLife	3.19%
Norfolk Southern Corp	3.19%



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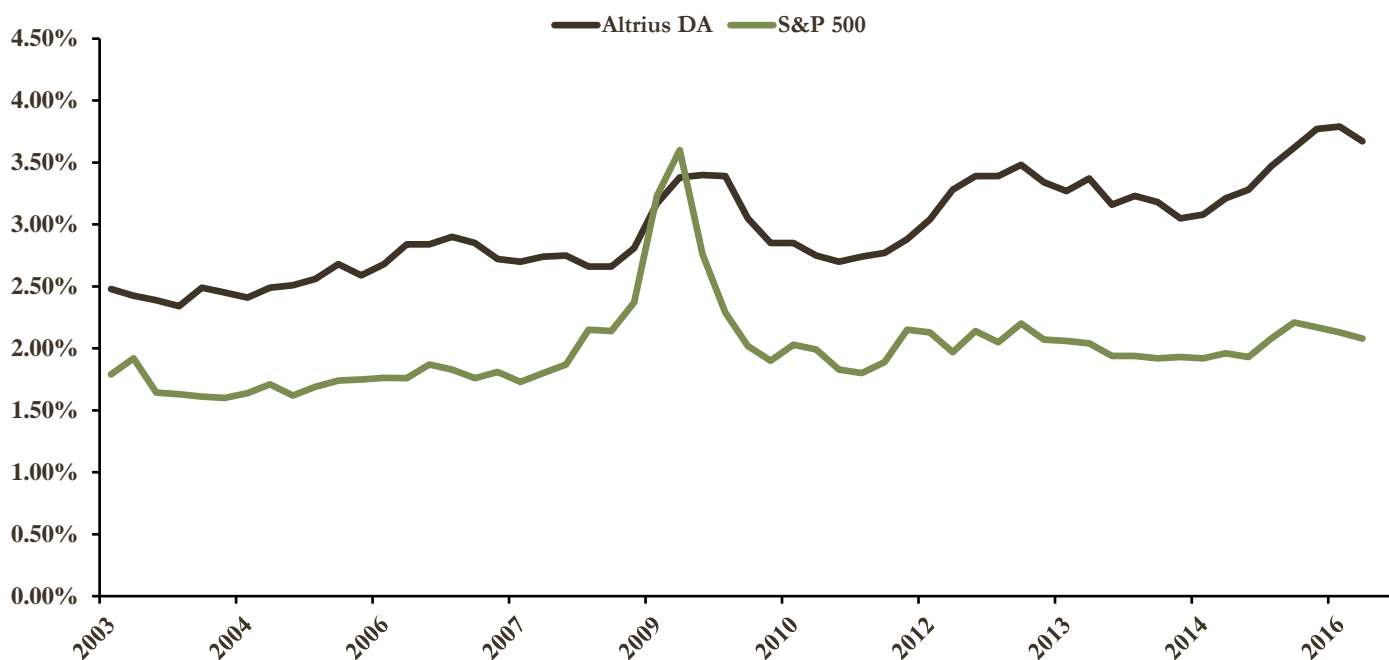
As one may recognize from the below chart, our firm has consistently provided a steady stream of income to our clients in the form of dividends. It is our assertion that this income stream has not only reduced the risk of our portfolio, but also provided a large part of the total return thereby leading to our performance success over this past tumultuous decade plus.

We believe that dividends allow our investors to “get paid to wait” while patiently working through volatile business and market cycles. This strategy provides emotional support during difficult cycles enabling investors to weather turbulent periods utilizing dividend income for personal needs or to reinvest cash at lower valuations. Our strategy is not only grounded in psychological and behavioral finance concepts, but is also supported by empirical evidence outperforming in both negative and full market cycles.

Dividends also act to align the interests of corporations and shareholders in helping to eliminate the agency effect. Corporate boards have recognized the value of dividends in stabilizing their stock price and encouraging investment during both high and lower tax regimes. In supporting and increasing dividends over time, managers are compelled to maintain a reliable stream of cash flows to shareholders rather than waste capital on those expenses adding little to corporate revenue including executive perks, pet projects, and ill-timed, unwise acquisitions. It appears a paradox; however, our experience and academic studies have displayed that sufficient investment for a good business can still occur in conjunction with dividends as managers are forced to invest cash flow more prudently and only in those capital investments in which they have the highest conviction in adding to corporate revenue particularly since stocks buybacks are often ill-timed.

**ALTRIUS: THIRTEEN YEARS OF CONSISTENT DIVIDENDS**

The strategy has consistently delivered a higher dividend yield than the S&P 500 since inception.



Source: Standard and Poor's



## DISCLOSURES

This report includes candid statements and observations regarding investment strategies, individual securities, and economic and market conditions; however, there is no guarantee that these statements, opinions or forecasts will prove to be correct. These comments may also include the expression of opinions that are speculative in nature and should not be relied on as statements of fact. Altrius is committed to communicating with our investment partners as candidly as possible because we believe our investors benefit from understanding our investment philosophy and approach. Our views and opinions include “forward-looking statements” which may or may not be accurate over the long term. Forward-looking statements can be identified by words like “believe,” “expect,” “anticipate,” or similar expressions. You should not place undue reliance on forward-looking statements, which are current as of the date of this report. We disclaim any obligation to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise. While we believe we have a reasonable basis for our appraisals and we have confidence in our opinions, actual results may differ materially from those we anticipate.

The information provided in this material should not be considered a recommendation to buy, sell or hold any particular security. The S&P 500<sup>®</sup> Index is an unmanaged index of 500 selected common stocks, most of which are listed on the New York Stock Exchange. The Index is adjusted for dividends, weighted towards stocks with large market capitalizations and represents approximately two-thirds of the total market value of all domestic common stocks. The Russell 1000 Value Index is an unmanaged index commonly used as a benchmark to measure value manager performance and characteristics. The Dow Jones U.S. Select Dividend Index is an unmanaged index commonly used as a benchmark to measure dividend manager performance and characteristics. The Russell 2000 Index, the Russell 2000 Growth Index, and the Russell 2000 Value Index are unmanaged indices commonly used as benchmarks to measure small cap manager performance and characteristics. The MSCI EAFE<sup>®</sup> Index is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the U.S. & Canada. The Barclays Capital U.S. Aggregate Bond Index and Bank of America Merrill Lynch US High Yield Master II Total Return Index are unmanaged indices that are commonly used as benchmarks to measure fixed income performance and characteristics. Index performance returns do not reflect any management fees, transaction costs or expenses. Investments cannot be made directly in an index. **Investments made with Altrius Capital Management, Inc. are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risks, including possible loss of the principal amount invested. Past performance is not a guarantee of future returns.**