The Dividend Value Discipline™
Quarterly Market Commentary
4th Quarter 2017 (Q4) – as of December 31st

We closed out 2017 well short of our objectives – most fully-invested accounts within **The Dividend Value Discipline™** pegged in with returns for 2017 in the +2.50% range, which is up from ~2% from the September 30th figures, but not near enough, especially in light of Canada's S&P/TSX Composite Index being up 6.03% and the U.S.'s S&P 500 Index being up 11.84% in Canadian dollar terms (19.42% in U.S. dollar terms). Due to our ***"buys only mandate"***, coupled with differences in start dates and timing of cash flows, no two accounts are exactly alike – your individual results can be found on **The Progress Monitor**. As always, all return figures are net of fees.

Our focus on dividend-paying stocks, coupled with our fixed income exposure, translates to a program that should outperform North American stock market indices during the weak years and underperform during the strong years. That said, 2017 marks the second calendar year in a row where returns in **The Dividend Value Discipline™** have been unacceptably low, so your **"elephant in the room"** questions likely are:

- **Why did you underperform?**

- **What are you doing to renew my faith in The Dividend Value Discipline™?**

To answer those questions, we have outlined our top challenges and importantly, our top successes for the year, along with the changes we are implementing to better the outcome for 2018 and beyond.

<u>**Top 2017 Challenges**…and what needs to change:</u>

- We were too early with the purchase of our low-cost commodity producers, Peyto, ARC Resources and Cameco – collectively, they took off 3.77% from our 2017 performance. What needs to be said is that the reasons we bought them are still valid. All three are ultra-low cost producers, led by industry veterans that are capable of surviving **any** prolonged industry downturn and profiting handsomely on the inevitable up cycle. Interestingly, they were our three strongest stocks on the first trading day of 2018, up 4.32%, 4.31% and 3.93%, respectively. What needs to change? Commodity producers by nature are trading opportunities, as opposed to "buy and hold" animals like say Microsoft, Starbucks and Scotiabank. Going forward, we intend to make better use of exchange-traded funds for exposure to commodities, which will allow us to devote more time to studying the long term value creators.

- The Canadian dollar started out the year at 74.39 cents U.S. and then moved in yo-yo fashion within a range of 72.48 cents U.S. in May to a high of 82.91 cents U.S. in September – a 14% swing from top to bottom. It closed out the year as a net headwind of 6.5% against the value of our U.S. dollar-denominated securities, so roughly -3.25% for the program. What needs to change? In our view, not much. We are comfortable with the roughly 50% exposure to the U.S. dollar that **The Dividend Value Discipline™** currently has. It is the earnings and dividend growth of our companies that will ultimately drive stock prices – currency headwinds and/or tailwinds have limits.

- It is now clear that our goal of an +8% return "each and every year" is working against us, i.e. when companies experience temporary setbacks, instead of buying more we have often ended up selling some of the position in an effort to deliver/protect the 8% by year-end. Conversely, we have also taken short-term profits on companies for the same reason, at the expense of even better returns in the long term. By way of example, we entered 2017 with a 2.5% position in Dollarama at an average cost of $79/share, and then sold roughly half of it at $100/share, only to watch it close out the year at $157 (and yes, we still own the other half). Why did we sell the first stake? Because we know that companies can and do have setbacks, and our goal was to deliver an 8% return by year-end. What needs to change? We need to take a long-term view in respect to our return goal, rather than trying to achieve it each and every year.

Top 2017 Successes...and what we need to do more of:

- We exited the year with the strongest group of companies we have ever owned. Most of our investee companies continue to grow their earnings and their rent cheques (dividends) at double-digit rates. Sooner or later, these increases are going to show up in the stock's price. To quote Benjamin Graham (mentor to Warren Buffett), "In the short term the market is a voting machine, in the long term it is a weighing machine", and investors ultimately weigh earnings and dividend growth. For a complete listing of our investee company rent cheque growth, please refer to the last page of this commentary.

- The transition to "disruptors and aggregators" got started in earnest in 2016. There were some notable winners in our portfolio (all figures in Canadian dollars): For 2017, Dollarama shares were up 59.6%, Sherwin-Williams was up 42.2%, both Intuit and Microsoft were up 28.3%, Constellation Software was up 24.9%, Lowe's was up 21.8%, Amphenol was up 21.7%, and Suncor was up 20%. Bottom line, we have demonstrated our ability to find great companies at reasonable value propositions – we just need to own them for longer periods.

- In 2017, we continued to acquire some truly great culture/wide moat companies that are aggregating and/or disrupting their competitors. Notable additions include Manulife Financial, Gilead Sciences, Northern Trust, Starbucks, Bank of the Ozarks, Skyworks Solutions, Stantec, and Nike. It is worth noting that the median 3-year dividend rate for the above companies is 14.9%, higher than the program median of 13.5%, so we are heading in the right direction. You can expect to see more of the same.

So what do these changes mean for you, our client?

For some, absolute returns each and every year is more important than the +8% over the long haul, and allocating more of your investments towards our GIC and/or preferred share strategies may be in order.

For most, we believe you will be best served with our humble dividend growers. Why? Downside performance is incredibly tough to recover from. A 20% loss means you need 25% upside just to get back even. It is in this realm where **The Dividend Value Discipline™** shines. If you have been with us since the inception of the program (September 2002), you have experienced one calendar year of negative performance – not surprisingly, that was 2008. Even with our subpar performance over the last couple of years, the annualized returns of these first accounts still range from a low of 6.8% to a high of 8.9%, over a 15+ year span. **The Dividend Value Discipline™** was always designed to be a Steady Eddy type of strategy – the kind that will keep you in the game for the long haul.

For a handful of clients, we recognize that **The Dividend Value Discipline™** is never going to allow you to participate in the Facebook, Amazon, Netflix, and Google's of the world and frankly, that drives you crazy. Assuming you have the risk tolerance, we have developed a few strategies over the past year which will allow you to access some.

In closing, please know this – Ryan and I have a huge vested interest in your personal financial success. If we thought it was time to throw in the towel on **The Dividend Value Discipline™**, then that is what we would do. The reality is we have acquired some truly exceptional companies that are growing their rent cheques at double-digit rates, and with the above noted changes we firmly believe we are on the cusp of substantially better results for a very long time to come. We are determined to make your personal financial success, your reality and look forward to our upcoming meetings.

Blessings to you and your family for a Happy New Year,

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Rent Cheques That Grow

	Company	Annual Rent Cheque	Yield	Last Dividend Change Announced*	3-Year Dividend CAGR	5-Year Dividend CAGR	Years to Double Rent Cheque**	Aggregator/ Disruptor?	Years of Consecutive Increases	Date of Last Dividend Change
1	SKYWORKS SOLUTIONS INC	$1.28	1.26%	14.0%	54.1%	n/a	1.6	Disruptor	2	21-Jul-17
2	STARBUCKS CORP	$1.20	2.01%	20.0%	32.1%	27.2%	2.5	Both	6	2-Nov-17
3	CCL INDUSTRIES INC CL B	$0.46	0.82%	15.0%	27.9%	24.1%	2.8	Both	15	21-Feb-17
4	LOWES COMPANIES INC	$1.64	1.73%	17.1%	26.0%	22.3%	3.0	Aggregator	54	21-Jul-17
5	INTUIT INC	$1.56	0.95%	14.7%	23.9%	20.3%	3.2	Disruptor	6	27-Jul-17
6	TJX COMPANIES INC	$1.25	1.62%	20.2%	23.1%	23.2%	3.3	Both	20	2-Apr-17
7	EXPEDIA INC	$1.20	0.94%	7.7%	22.0%	22.2%	3.5	Disruptor	5	6-Mar-17
8	CVS HEALTH CORP	$2.00	2.55%	17.6%	22.0%	25.1%	3.5	Aggregator	9	20-Jan-17
9	AMPHENOL CORP	$0.76	0.85%	18.1%	19.1%	29.3%	4.0	Aggregator	5	26-Jul-17
10	BANK OF THE OZARKS	$0.76	1.51%	9.1%	17.4%	24.9%	4.3	Aggregator	7	2-Oct-17
11	NIKE INC	$0.80	1.25%	11.0%	17.0%	16.4%	4.4	Disruptor	9	16-Nov-17
12	SHERWIN WILLIAMS CO	$3.40	0.81%	1.2%	15.6%	16.9%	4.8	Aggregator	38	15-Feb-17
13	AMERISOURCEBERGEN CORP	$1.52	1.59%	4.1%	15.2%	20.4%	4.9	Neither	12	9-Nov-17
14	MICROSOFT CORP	$1.68	1.90%	7.6%	13.5%	15.1%	5.5	Both	13	19-Sep-17
15	MANULIFE FINANCIAL CORP	$0.82	3.07%	11.0%	12.9%	9.5%	5.7	Neither	3	9-Feb-17
16	DOLLARAMA INC	$0.44	0.29%	10.0%	12.4%	15.9%	5.9	Disruptor	6	30-Mar-17
17	MARSH & MCLENNAN COS INC	$1.50	1.81%	10.3%	12.3%	10.8%	6.0	Aggregator	7	1-May-17
18	STANTEC INC	$0.50	1.43%	11.1%	10.6%	10.8%	6.9	Aggregator	4	1-Feb-17
19	GILEAD SCIENCE INC	$2.08	2.79%	10.6%	10.0%	n/a	7.3	Aggregator	2	7-Feb-17
20	NORTHERN TRUST CORP	$1.68	1.65%	10.0%	8.4%	7.0%	8.6	Neither	6	19-Jul-17
21	SUNCOR ENERGY INC	$1.28	2.73%	10.3%	7.9%	20.7%	9.2	Neither	1	2-Feb-17
22	BANK OF NOVA SCOTIA (THE)	$3.16	3.83%	3.9%	7.3%	7.1%	9.9	Disruptor	6	29-Aug-17
23	GREAT WEST LIFECO INC	$1.47	4.20%	6.1%	6.0%	3.6%	11.9	Aggregator	2	10-Feb-17
24	PEYTO EXPLORATION & DEVELOPMENT CORP	$1.32	9.43%	0.0%	0.0%	12.9%	n/a	Neither	0	15-Nov-14
25	CONSTELLATION SOFTWARE INC***	$5.01	0.69%	0.0%	0.0%	0.0%	n/a	Aggregator	0	15-Mar-10
26	ARC RESOURCES LTD	$0.60	4.10%	0.0%	-20.6%	-12.9%	n/a	Neither	0	10-Jan-10
27	CAMECO CORPORATION	$0.08	0.66%	-80.0%	-41.5%	-27.5%	n/a	Neither	0	10-Nov-17
	Median		**1.62%**	**10.29%**	**13.47%**	**16.36%**	**4.8**		**6.0**	

*Or 0% if no dividend change in the last 12 months.

**Based on 3-year Dividend CAGR (Compound Annual Growth Rate) - as of January 5, 2018

***Constellation Software's dividend rate is in USD ($1.00 per quarter), but the payments are made in CAD and therefore vary with currency fluctuations

Prepared by Chris Raper & Associates