

DM Monthly Report

SUMMER 2017

PORTFOLIO ACTIVITY

Last month, we sold long time hold-ing Home Capital Group from the DM Canadian Equity Portfolio and opened a new position in Colfax Corp. in DM Foreign Equity.

FEATURE STOCK

Rogers Communications (RCI.B)

In 2014, Joe Natale assumed the role of CEO at Telus Corp. and, over the ensuing two plus years, was credited with vastly improving the company's deficient customer service offering. For personal reasons, however, Mr. Natale wished to return to his native Toronto, giving RCI the opportunity to hire the executive away to replace their own retiring CEO. Last month, Natale hosted his first RCI earnings call and outlined his three key areas of focus for the quarters ahead: (1) improving customer service, just as he had done at Telus, (2) establishing an organizational structure that fosters a culture of accountability, and (3) strengthening the company's cost management discipline. Shortly after the call, analysts suggested that the targeted operational improvements could lift revenues and earnings by as much as 3-5%, with cash flow potentially boosted by an even greater degree. Not including dividends, RCI shares have appreciated by more than 20% so far this year.

FOCUS ON INTRINSIC GROWTH, LET PRICE FOLLOW

In presentations to clients and prospective clients, we spend significant time discussing company cash flow and why this metric is so important within our investment process. From our perspective, firms that are generating (and especially growing) excess cash have a relatively quantifiable intrinsic value and don't require us to rely as much on possible future corporate developments for investment return, events which regularly fall short of market expectations. In our analysis, executives at companies producing cash above what is required to maintain their business may elect to do one or more of 4 things with this capital: *they can acquire other firms or assets; they can buy back shares; they can invest internally to boost organic growth; or they can pay dividends.* From a shareholder's perspective, the most visible and perhaps most certain of these options is the dividend. The stocks of companies with strong dividend policies offer several benefits: they pay us while we await share price appreciation; the regular income they offer – especially in a low interest rate environment – can help to limit downside; and, if management is consistently raising the dividend, the underlying value of the position should also be climbing over time.

In the DM Canadian Equity Portfolio, one of our greatest long term dividend performers has been CN Rail. Due partly to its oligopolistic nature and resulting pricing power, and partly to management's operational effectiveness, CN has been able to grow cash flow on a very consistent and robust basis for several years. Though some of this capital has been deployed to other purposes, a significant portion has been returned to shareholders through dividend growth. The chart at bottom left highlights this history, showing that CN's dividend per share has risen nearly fourfold over the past decade, or at a compound annual rate of about 15%. As the chart to the right shows, CN share price has roughly followed this trend. That's not to say that appreciation has been uninterrupted, though, and as the grey shaded portions indicate, there have been long stretches during which the stock did nothing. Knowing that cash flow (and corresponding intrinsic value) was growing, however, has helped us to wait patiently for eventual price gains.

