Prescribing a New Addition

Target Corp. (TGT) is being deleted from the portfolio to make room for CVS Health (CVS).

CVS Health (CVS), known for its drug stores, also realizes significant revenues from administering drug benefits for health plans. Over the last five years, CVS has increased its dividend at an annualized rate of 27.7%. The company is committed to returning cash to shareholders and has an attractive dividend yield of 2.6%, well above its historical average of 1.5%.

More information about the deletion and addition can be read in the DI Portfolio Alerts section.

A Very Good First Quarter

The S&P 500 index ended the first quarter of 2017 with its biggest quarterly gain since the end of 2015. The strongest-performing sector of the quarter was by far technology, which gained 12% in the first three months of the year (as measured by technology stocks within the S&P 500). The NASDAQ Composite ended the first quarter up 9.8%, its best quarter since 2013. Recent positive economic reports have investors betting that the technology sector will benefit from stronger economic growth.

Despite the strong quarterly performance, U.S. markets took somewhat of a breather in March, as investors began to question the new administration’s ability to enact new legislation in a timely manner. Much of the recent rally—or the “Trump rally,” as some have called it—is fueled by expectations that the new administration would be able to implement a corporate tax overhaul, loosen regulations and increase fiscal spending.

Recent positive performance can also be attributed to improving corporate earnings. As we head into April and kick off second-quarter earnings season, the focus will again be on corporate earnings. While Barron’s puts the current price-earnings ratio (P/E) for the S&P 500 at 26.5, if earnings begin to increase, valuations may come down. Earnings are the denominator of the P/E ratio; if the denominator increases, the overall ratio will decline (if prices hold steady). If earnings are able to increase at a faster clip than prices, current market valuations may become less rich compared to historical averages. However, disappointing results could ignite concerns that stock price gains have outpaced earnings growth.

Analysts polled by Thomson Reuters anticipate that S&P 500 reported first-quarter 2017 earnings to have increased 10.1%, compared to the first quarter of 2016. Energy sector companies are expected to post the largest year-over-year increase of 604.8% (prior-year earnings were negative), followed by financials with a 15.4% increase, and materials and technology with projected increases of 14.8% and 14.7%, respectively. Only three sectors are expected to show year-over-year quarterly earnings declines for the first quarter: industrials (with anticipated earnings down 5.6%), telecommunications (a 2.8% decline) and consumer discretionary (a 1.4% decline).

Despite the positive sentiment, analysts have trimmed their expectations for earnings growth since the start of the year; at the beginning of 2017, analysts...
Portfolio Alerts This Month

### April Portfolio Deletions

<table>
<thead>
<tr>
<th>Company (Ticker)</th>
<th>Portfolio Deletion Alert Date</th>
<th>Portfolio Addition Alert Date</th>
<th>Stock Total Return Since Purchase*</th>
<th>Index Total Return Since Purchase*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target Corporation (TGT)</td>
<td>4/7/2017</td>
<td>12/31/2011</td>
<td>21.4%</td>
<td>97.6%</td>
</tr>
</tbody>
</table>

Add the DI portfolio on January 3, 2017.

### April Portfolio Additions

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>CVS Health (CVS)</td>
<td>$77.87</td>
<td>2.6%</td>
<td>Services: Retail (Drugs)</td>
</tr>
</tbody>
</table>


pollled by Thomson Reuters expected first-quarter S&P 500 earnings to increase 13.8%.

Revenue is also expected to pick up for the first quarter. Thomson Reuters’ consensus estimate calls for revenue growth of 7.0%, which would be the biggest aggregate jump in more than five years.

Earnings growth is important to dividend investors, because ultimately if a company isn’t profitable it will not be able to sustain its dividend payment. While executives are hesitant to cut dividend distributions, that doesn’t guarantee continuation of dividend payments. If a company is continually paying out more than it is earning (an earnings payout ratio over 100%), it will not be able to sustain the payment and will ultimately have to cut its distribution or eliminate it altogether.

### DI Portfolio Alerts

There is one portfolio deletion and one portfolio addition for April. Target Corp. (TGT) is being deleted from the portfolio and CVS Health (CVS) is being added.

**Portfolio Deletion: Target Corp. (TGT)**

Target has gained 21.4% since being added the DI portfolio on January 3, 2012. This gain is far below the 97.6% total return realized by the Dow Jones U.S. Index ETF (IYY) over the same period. The retailer was among the DI portfolio’s original holdings.

Target is being removed because of headwinds and uncertainty facing its business model going forward. In a meeting with Wall Street analysts following the company’s earnings conference call in March, Target provided some detail on the investments and changes it will be making to deal with the “new era” in retail. The investments include $1 billion in operating margins in 2017 to ensure prices are competitive, revamping more than 100 stores and other efforts. The retailer will invest more than $7 billion over the next three years with plans to update more than 600 stores and open more than 100 small-format stores by 2019 and introduce more than 12 new brands over the next two years. The company has signaled that it is willing to sacrifice gross margins to boost traffic as it faces stiff competition from the likes of Amazon.com (AMZN) and Wal-Mart Stores (WMT).

“While the transition to this new model will present headwinds to our sales and profit performance in the short term, we are confident that these changes will best position Target for continued success over the long term,” CEO Brian Cornell said.

Additionally, the company has stated that it is targeting a 40% payout ratio. Currently, the company pays out 49% of GAAP earnings as dividends. While it is not believed that the company would cut its dividend, future dividend increases are expected to be well below historical increases, especially when earnings have only been growing by an average of 1.4% per year over the last five years.

The company’s recent and steep price decline keeps its dividend yield attractive on a relative basis. The current yield is 4.5%, above the five-year average of 2.7%. It is Target’s investment profile that is prompting its deletion.

**Portfolio Addition: CVS Health (CVS)**

CVS Health is an integrated pharmaceutical health care company. CVS operates in three segments: pharmacy services, retail/long-term care (LTC) and corporate. The pharmacy services segment provides a range of pharmacy benefit management (PBM) solutions to its clients. Also in the pharmacy services segment is CVS’ SilverScript Insurance subsidiary—a national provider of drug benefits under the Medicare Part D program. CVS is expanding its specialty pharmacy services (support for individuals who require complex and expensive drug therapies) and currently has a...
leading stand-alone Medicare Part D prescription drug plan.

As of December 31, 2016, the retail/LTC segment included 9,709 retail locations (of which 7,980 were its stores that operated a pharmacy and 1,674 were its pharmacies located within Target stores), its online retail pharmacy websites, 38 onsite pharmacy stores, its long-term care pharmacy operations and its retail healthcare clinics.

CVS is unique in that it is vertically integrated by having an independent PBM to process claims in addition to having a pharmacy retail store.

Prescription benefit managers (PBMs) are third-party administrators of prescription drug programs for commercial health plans (self-insured employer plans, Medicare Part D plans, state government employee plans or traditional company benefit plans). A PBM is responsible for contracting with pharmacies, negotiating discounts and rebates with drug manufacturers and processing and paying prescription drug claims, among other things. As of 2016, PBMs manage pharmacy benefits for 266 million Americans.

CVS processes 1.4 billion adjusted claims annually, which gives it significant scale advantages [CVS is the largest prescription benefit manager behind Express Scripts (ESRX)]. Because of its scale, CVS has been able to negotiate significant drug pricing discounts with suppliers, making its services more attractive to prospective clients.

Aside from a competitive advantage, CVS is fundamentally attractive. The stock’s 24% price decline over the last year has lowered the trailing price-earnings ratio to 15.8, below the five-year average of 18.1. The stock’s forward price-earnings ratio based on expected 2017 earnings is even more attractive at 13.3. CVS’ current dividend yield of 2.6% is far above its five-year average of 1.5%. The increase in the yield is due to its recent price decline, but the yield has also been boosted by the company’s significant dividend growth. Over the last five years, CVS has grown its dividend at an average annualized rate of 7.7%.

The company’s current earnings payout ratio of 34.3% is above the five-year average of 27.4%, but remains relatively low. CVS announced that it will be targeting a 35% earnings payout ratio by 2018, but also noted in its most recent earnings conference call that its current payout ratio is “artificially high as it includes the integrated cost related to both Omnicare and Target [deals], as well as other items described in our non-GAAP reconciliation on our website.” The company also reiterated its commitment to growing the dividend in the future. At the end of 2016, CVS had $18.2 billion left in authorizations for share buybacks.

CVS is not without its risks. The PBM model has recently been under scrutiny, particularly with regard to their profit models and lack of transparency. CVS recently defended itself in its fourth-quarter 2016 earnings conference call: “We are the solution and not the problem. And that’s why both public and private payers continue to count on PBMs as indispensable partners that help to manage their drug trend.” Many analysts have reiterated that they agree with CVS on the benefits of PBMs and that the market’s concern is overdone.

CVS also faced headwinds last year when Prime Therapeutics, owned by Blue Cross Blue Shield, announced that CVS will no longer be in its preferred network. The Department of Defense’s

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Company</th>
<th>Portfolio Alert Date</th>
<th>DI Purchase Price</th>
<th>Latest Price (4/4/17)</th>
<th>Mar Gain/ (Loss)</th>
<th>Total Return Since Purchase</th>
<th>Div Yield</th>
<th>Industry</th>
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<tbody>
<tr>
<td>AAPL</td>
<td>Apple Inc.</td>
<td>4/4/14</td>
<td>$75.97</td>
<td>$75.27</td>
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<td>CAT</td>
<td>Caterpillar Inc.</td>
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<td>$101.76</td>
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<td>CRL</td>
<td>Cracker Barrel</td>
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<td>$158.50</td>
<td>$158.80</td>
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<td>Restaurants</td>
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<td>CMI</td>
<td>Cummins Inc.</td>
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<td>$136.18</td>
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<td>18.8%</td>
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<td>CVS Health</td>
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<td>na</td>
<td>(2.6%)</td>
<td>na</td>
<td>2.6%</td>
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<td>Eastman Chemical Co.</td>
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<td>19.3%</td>
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<td>ETN</td>
<td>Eaton Corporation</td>
<td>12/3/11</td>
<td>$43.53</td>
<td>$45.52</td>
<td>3.9%</td>
<td>95.4%</td>
<td>96.3%</td>
<td>Electronic Instruments &amp; Controls</td>
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<td>EMR</td>
<td>Emerson Electric Co.</td>
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<td>7.3%</td>
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<td>IBM Corp.</td>
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<td>$145.94</td>
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<td>International Paper Co.</td>
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<td>$45.81</td>
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<td>IVZ</td>
<td>Invesco Ltd.</td>
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<td>$38.18</td>
<td>$38.82</td>
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<td>11.8%</td>
<td>26.5%</td>
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<td>MDT</td>
<td>Medtronic PLC</td>
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<td>$72.87</td>
<td>$75.05</td>
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<td>8.6%</td>
<td>4.3%</td>
<td>Medical Equipment &amp; Supplies</td>
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<td>OXY</td>
<td>Occidental Petroleum</td>
<td>1/9/15</td>
<td>$77.54</td>
<td>$76.96</td>
<td>(0.2%)</td>
<td>(7.5%)</td>
<td>20.7%</td>
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<td>PEP</td>
<td>PepsiCo, Inc.</td>
<td>12/31/11</td>
<td>$66.35</td>
<td>$66.66</td>
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<td>Polaris Industries Inc.</td>
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<td>$86.34</td>
<td>(1.7%)</td>
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<td>4.3%</td>
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<td>PFG</td>
<td>Principal Financial Group</td>
<td>12/9/16</td>
<td>$60.30</td>
<td>$59.55</td>
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<td>4.3%</td>
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<td>PGR</td>
<td>Procter &amp; Gamble Co.</td>
<td>12/7/12</td>
<td>$70.29</td>
<td>$70.89</td>
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<td>45.1%</td>
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<td>RHI</td>
<td>RHI International</td>
<td>10/7/16</td>
<td>$37.66</td>
<td>$37.93</td>
<td>1.2%</td>
<td>22.4%</td>
<td>10.6%</td>
<td>Business Services</td>
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<tr>
<td>TXN</td>
<td>Texas Instruments</td>
<td>4/5/13</td>
<td>$34.20</td>
<td>$34.80</td>
<td>5.1%</td>
<td>157.9%</td>
<td>61.4%</td>
<td>Semiconductors</td>
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<td>UNP</td>
<td>Union Pacific Corp.</td>
<td>7/2/15</td>
<td>$96.66</td>
<td>$97.23</td>
<td>(0.9%)</td>
<td>15.2%</td>
<td>16.9%</td>
<td>Aerospace and Defense</td>
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<td>UTX</td>
<td>United Technologies</td>
<td>10/7/16</td>
<td>$100.58</td>
<td>$99.10</td>
<td>112.99</td>
<td>(0.3%)</td>
<td>15.4%</td>
<td>Railroads</td>
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<td>WEC</td>
<td>WEC Energy Group</td>
<td>12/31/11</td>
<td>$34.96</td>
<td>$34.68</td>
<td>0.6%</td>
<td>131.2%</td>
<td>96.3%</td>
<td>Electric Utilities</td>
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<td>WSM</td>
<td>Williams-Sonoma, Inc.</td>
<td>6/3/16</td>
<td>$53.25</td>
<td>$54.00</td>
<td>10.4%</td>
<td>2.8%</td>
<td>13.8%</td>
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<td>WYN</td>
<td>Wyndham Worldwide Corp.</td>
<td>3/4/16</td>
<td>$76.04</td>
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<td>2.0%</td>
<td>15.7%</td>
<td>22.5%</td>
<td>Hotels &amp; Motels</td>
</tr>
</tbody>
</table>

Performance of DI Portfolio

TRICARE program also dropped CVS from its preferred network. The change means that a portion of Blue Cross insurance customers who use CVS pharmacies may pay a higher co-pay amount (or in some cases the entire prescription amount) to fill their prescription at CVS. These network changes may result in CVS losing 40 million prescriptions (out of 1.4 billion). The company’s prescription losses are primarily driven by

exclusive networks that Walgreens has arranged with other players in the drug chain to let patients get their prescriptions at a discount, reducing the need for CVS’ network in most cases. Analysts believe CVS will be able to bounce back from this and maintain its competitive advantage going forward. The company is confident that its menu of pharmacy, long-term care MinuteClinic and infusion services makes CVS Pharmacy a partner of choice for health plans and all PBMs, not just their own PBM.

For more on CVS, see pages 8 and 9.

March DI Performance

The DI tracking portfolio was unchanged in March. The 0.0% return consisted of a capital loss (price decline) of 0.5% and income return (dividend payments) of 0.5%. The portfolio’s benchmark, the Dow Jones U.S. Index ETF (IYY), had a total return of 0.1% in March, composed of a 0.3% capital loss and 0.4% income return. The IYY will not distribute its next dividend payment until the end of June.

Year to date, the DI tracking portfolio has gained 3.9%, compared to the IYY’s total return of 5.4%. Because the DI portfolio has a dividend investing emphasis, the expectation is that the tracking portfolio will lag the benchmark during bullish market periods, but decline less during periods of market turbulence. Over time, dividend income is expected to have an increasing (and positive) impact on the portfolio’s long-term performance. The DI portfolio’s weighted dividend yield of 3.5% is well above the Dow Jones U.S. Index ETF yield of 1.7%.

Portfolio News

Strongest Stocks in March

After climbing 10.4% in March, Williams-Sonoma Inc. (WSM) is the top performer in the DI portfolio for March. On March 15, the company announced quarterly earnings that beat the consensus estimate by 3%. For fiscal 2017, the company is forecasting total net revenues of $5.2 billion to $5.3 billion and comparable brand revenue growth of 1% to 3%. In addition, diluted earnings per share is expected to be between $3.45 and $3.65.

Williams-Sonoma declared a 5.4% increase in its quarterly cash dividend, from $0.37 to $0.39 per common share. The dividend is payable on May 26, 2017, to shareholders of record as of the close of business on April 28, 2017. This 5.4% increase is in line with last year’s 5.7% increase. The indicated
annual cash dividend is $1.56 per common share. This translates into a current yield of 2.9%, which is above the five-year average yield of 2.2%.

Texas Instruments (TXN) was the second-best performer in the DI portfolio during March, gaining 5.1%. There was a lack of company-specific news to explain the rise, but technology stocks in general outperformed during March.

At the end of January, Texas Instruments reported fourth-quarter earnings that beat analysts’ expectations. Quarterly revenue increased 7%, compared to the fourth quarter of 2015, as demand for Texas Instruments’ products remained strong in the automotive market. Throughout the third and fourth quarter of 2016, Texas Instruments saw improvement in its industrial end markets, while demand in the personal electronics market was down slightly from the fourth quarter of 2015. During 2016, Texas Instruments returned $3.8 billion to shareholders through stock repurchases and dividends, consistent with the company’s strategy to return all its free cash flow plus proceeds from exercises of equity compensation minus net debt retirement. Over the last 12 months, the company’s dividends have represented 40% of free cash flow.

Texas Instruments has gained 157.9% since being added the DI portfolio (on April 8, 2013), compared to the benchmark Dow Jones U.S. Index ETF’s gain of 61.4% over the same period. Despite the strong price appreciation, Texas Instruments’ dividend yield of 2.5% is only slightly below its five-year average of 2.6%, due to strong dividend growth. Over the last five years, Texas Instruments has increased its quarterly dividend at an annualized rate of 24.0%.

Apple Inc. (AAPL) was the third-best-performing stock in the DI portfolio during March, gaining 4.9%. The company has benefited from overall positive sentiment surrounding the technology sector, but has also been on a tear since its fourth-quarter 2016 earnings announcement in February.

At the end of March, the Australian government’s competition regulator barred the country’s largest banks from bargaining collectively for access to Apple’s contactless payment function. This decision is the first of its kind relating to new “tap-and-go” technology that uses radio-frequency identification (RFID) to make fast payments securely with a card. Banks will not be able to introduce their own mobile applications on devices such as the iPhone and Apple Watch that could be used for contactless payments in lieu of the Apple Wallet app. Banks favor developing their own apps to avoid transaction fees and they believe more customers would engage more frequently with bank-created apps.

Apple’s current dividend yield of 1.6% is the lowest in the DI portfolio. However, it remains above the five-year average low of 1.4%. In the past, Apple increased its quarterly dividend in April.

Eaton Corp. (ETN) was among the top performers in the DI portfolio during March, gaining 3.9%. There was no company specific news to attribute the stock’s performance to. During February, the company reported earnings that beat analysts’ expectations and reported that quarterly revenue fell 3.8% compared to the fourth quarter of 2015. While the company lowered its earnings guidance for the first quarter of 2017, it reiterated its full-year 2017 earnings expectations to be between $4.30 per share and $4.60 per share. Analysts polled by Thomson Reuters expect full-year 2017 earnings of $4.44 per share. Eaton expects organic revenue to be flat in 2017, but expects growth to accelerate in 2018.

Toward the end of February Eaton increased its dividend payment 5.3%, which is higher than the 3.6% increase announced in February of 2016. Eaton’s current dividend yield of 3.2% is in line with its five-year average.

For more on Eaton Corp., see pages 12 and 13.

Weakest Stocks During March

Invesco Ltd. (IVZ) was the worst-performing stock in the DI portfolio for the month, losing 4.8% of its value in March. The stock fell in lockstep with many other financial stocks mid-month. The drop started two days after the Federal Open Market Committee raised interest rates. Neither Invesco nor the Financial Select SPDR ETF (XLF) recouped their respective losses afterward.

None of the company-specific news for Invesco explains the decline. Assets under management rose 1.4% in February. Earnings estimates were unchanged. New SEC rules regarding ETFs following indexes with assets that are thinly traded should have little impact on Invesco.

The valuation continues to be attractive. Shares of Invesco yield 3.7%. This yield is above the five-year average high of 3.6%. The price-earnings ratio of 14.7 compares to a five-year average low of 15.6.

Invesco should report late this month. A dividend increase is expected to be included in the first-quarter earnings release.

Caterpillar Inc. (CAT) declined 4.0% during March. On March 2, law enforcement authorities entered three Peoria, Illinois, Caterpillar facilities, including the corporate headquarters, to execute a search and seizure warrant. The warrant is focused on the collection of documents and electronic information. Caterpillar is cooperating with law enforcement.

In a press release, Caterpillar said it believes the execution of the search warrant is regarding, among other things, export filings that relate to CSARL, the company’s Switzerland subsidiary. The company first disclosed the matter in its Form 10-K filed on February 17, 2015, and updated it in its

Recent Earnings Announcements

<table>
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<tr>
<th>Ticker</th>
<th>Company</th>
<th>Date Reported</th>
<th>Reported Earnings</th>
<th>Expected Earnings</th>
<th>Surprise %</th>
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<tbody>
<tr>
<td>WSM</td>
<td>Williams-Sonoma, Inc.</td>
<td>Mar 15</td>
<td>$1.550</td>
<td>$1.505</td>
<td>3.0%</td>
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</table>

most recent Form 10-K filed with the SEC on February 15, 2017. A spokeswoman for the attorney’s office cited that agents from the U.S. Department of Commerce, Internal Revenue Service and Federal Deposit Insurance Corp. were behind the searches. No arrests were made.

Following the facility raids, Caterpillar CEO Jim Umpleby apologized to the company’s employees; in a memo he said, “We were surprised by today’s actions primarily because we have been so cooperative with the authorities in this investigation. We will continue to work toward a resolution of these matters, just as we did today. Because of the broad nature of today’s warrant, we don’t have enough information at this time to provide a full understanding of the authorities’ intent.”

In other news, Caterpillar announced that it is closing its facility near Aurora, Illinois, and laying off 800 workers.

Earlier this year, the company said it would lay off employees in 2017 because of an anticipated decline in demand for its products.

**International Paper Co. (IP)** was among the worst-performing stocks in the DI portfolio during March, losing 3.6%. There was no company-specific news pertaining to the price decline.

International Paper has declined by 5.7% since the start of 2017. Despite the decline, International Paper’s trailing price-earnings ratio is 23.1, while its forward price-earnings ratio is 13.9 times expected full-year 2017 earnings of $3.64 per share.

**IBM Corp. (IBM)** lost 3.2% in March. There was no negative company-specific news during March causing the decline. During March, IBM announced a partnership with Salesforce.com (CRM) to share their respective artificial-intelligence (AI) technologies. The goal of this partnership is an AI service that integrates the learning capabilities of IBM’s Watson with the sales-focus of Salesforce’s Einstein. Essentially, Watson could be used to predict local spending patterns based on the raw business data that Einstein collects and processes.

IBM had a previous relationship with Salesforce through Bluewolf Group, a consulting service specializing in Salesforce’s services, which IBM acquired in 2016. This acquisition led to the current collaboration. For IBM, the collaboration further pushes its AI technology into the business and cloud services market, where it sees its future core business heading. Salesforce’s customer service software will also be adopted by IBM companywide as part of the deal. The companies are not sharing revenue, but hope that their services will reach more customers due to the partnering capabilities of their products.

IBM’S dividend yield of 3.2% is above its five-year average of 2.6%.
Dividend Analysis

<table>
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<tr>
<th>Ticker</th>
<th>P/E Ratio (TTM)</th>
<th>Dividend Yield</th>
<th>Est EPS Growth Rate</th>
<th>Div Growth Rate</th>
<th>First Year Div Paid</th>
<th>Consecutive Years Div Raised</th>
<th>Payout Ratio: EPS</th>
<th>Payout Ratio: FCFPS (12 Month)</th>
<th>Liab to Assets</th>
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An"l Ind Div: The total dollar amount of cash dividends forecast to be paid over the next 12 months.
Consecutive Years Div Raised: The number of current years the company has continuously increased the annual dollar amount of the dividend.
Date Payable: The date a company will distribute (or has distributed) the most recent quarterly dividend.
DI Purchase Price: The average cost basis per share of the stocks purchased for the real DI tracking portfolio. The average cost basis includes any commissions incurred for the purchase and is adjusted for stock splits and spin-offs, if appropriate.
Direct Invest: Denotes companies that offer a direct investment program, which allows investors to buy their initial shares directly from a company, without having to go through a broker.
Div Growth Rate (5 Yr): The compound annual percentage change in dividends per share over the past five years. Positive numbers show an increase in the dollar amounts of dividends paid.
Div Yield (or Current Dividend Yield): Projected dividend payments for the next 12 months divided by the current stock price. This number shows, in percentage form, how much income can be expected relative to the current stock price.
Dividend Yield—1 Year Ago: The stock's dividend yield (dividends divided by price) from one year ago. **5 Year Average**: The stock's average dividend yield over the past five years.
Div Growth Rate (3-5 Yr): The forecast annual growth rate in earnings per share for the next three to five years.
Ex-Dividend Date: The date used by the exchanges to determine who owns shares of a company. This is two trading days before the record date. Investors must purchase shares prior to the ex-dividend date to receive the dividend.
First Year Dividend Paid: The first year a company paid its dividend. If a dividend was suspended, the date is the first year the dividend was reinstated.
First Year Dividend Paid: The first year a company paid its dividend. If a dividend was suspended, the date is the first year the dividend was reinstated.
Liab to Assets: Total liabilities divided by total assets. A measure of balance sheet strength. A lower percentage indicates a lower proportionate amount of debt.
Market Cap (Mil): A measure of company size, this is the current share price multiplied by the number of shares outstanding, expressed in millions of dollars.
Months Dividends Paid: The calendar months the company has typically paid dividends to shareholders (1 = January, 2 = February, 3 = March, etc.).

Definitions of Terms Used in Tables

- **DRIP Plan**: Denotes companies that offer a dividend reinvestment plan, which allows shareholders to use cash dividends to acquire additional shares of stocks, including partial amounts.
- **Est EPS Growth Rate (3-5 Yr)**: The forecast annual growth rate in earnings per share for the next three to five years.
- **First Year Dividend Paid**: The first year a company paid its dividend. If a dividend was suspended, the date is the first year the dividend was reinstated.
- **Liab to Assets**: Total liabilities divided by total assets. A measure of balance sheet strength. A lower percentage indicates a lower proportionate amount of debt.
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- **Months Dividends Paid**: The calendar months the company has typically paid dividends to shareholders (1 = January, 2 = February, 3 = March, etc.).
- **Payment Amount**: The dollar amount of the current quarterly dividend payment. An up arrow (↑) indicates that the dividend is higher than that paid last quarter. If no arrow is displayed, the dividend has not changed from the prior quarter.
- **Payout Ratio**: EPS—12 Month: The average payout ratio for the previous five years. The percent- age of earnings paid out as dividends over the latest 12-month period.
- **Payout Ratio**: FCFPS (12 Month): The percentage of free cash flow per share paid out as dividends over the latest 12-month period. Free cash flow is cash flow from operating activities less capital expenditures. A measure of a company's ability to both pay dividends and increase its cash balance.
- **P/E Ratio (TTM)**: The price-earnings ratio (price divided by earnings) based on reported earnings per share for the previous 12 months (trailing 12 months).
- **Total Return Since Purchase—Stock**: The change in a stock's price plus the value of all dividends received during the holding period divided by the commission-adjusted purchase price.
- **Index**: The total return of the benchmark index since the stock was added to the DI tracking portfolio, expressed as a percentage.

April 2017
CVS Health (CVS)

CVS Health is the largest U.S. pharmacy, based on total prescription revenue. The company has more than 9,700 retail locations and over 1,100 walk-in medical clinics. CVS is also a leading pharmacy benefits manager (PBM) with nearly 90 million plan members. The company’s drug stores offer prescription drugs and an assortment of general merchandise, including OTC drugs, beauty products and cosmetics, film and photo finishing services, seasonal merchandise, greeting cards and convenience foods. CVS’ pharmacy services segment provides a range of pharmacy benefit management (PBM) services, including the operation of mail order pharmacies, specialty pharmacies, Medicare Part D services, formulary management and discounted drug purchase agreements. CVS is also the largest operator of retail health clinics in the U.S. under the MinuteClinic name.

Why Own CVS?

CVS operates one of the largest drug store chains and pharmacy benefit managers in the U.S. and is also the largest operator of retail health clinics, having acquired Target’s pharmacy business in December 2015 for approximately $1.9 billion. The company also acquired Omnicare, a prescription drug and service provider to the long-term health and specialty health care industries in August 2015 for a total enterprise value of $12.7 billion. The company’s substantial scale includes 24% market share in the retail pharmacy prescription market in 2016, 31% of the PBM prescription market, 28% of the specialty pharmacy market, and 23% share of the long-term care (LTC) prescription market.

Recent worries about the impact of existing health insurance laws and the move by health insurers to restrict choices of pharmacies have pushed CVS shares down roughly 24% over the last year. As a result, the current price-earnings ratio is 15.8 times trailing earnings per share of $4.93. Based on the consensus earnings estimate of $5.87 for the current fiscal year ending December 31, the forward price-earnings ratio is 13.3 and is 12.2 times fiscal-2018 projected earnings. These ratios are attractive relative to the industry, which has averaged 21.3 over the last five years, and relative to the company’s average price-earnings ratio of 18.1.

Since 2012, the company has generated $26 billion in net new PBM business and 2,200 net new pharmacy locations. Over the last five years fully diluted earnings from continuing operations have grown, on average, by 13.6% per year, while sales have risen an average of 10.6% over the same period. Five analysts polled by I/B/E/S are forecasting earnings growth of 11.7% per year for the next three to five years, ranging from a low of 6.7% to a high of 20.4%.

On February 9, the company reported quarterly earnings of $1.71 per share, which beat the consensus estimate by 2.5%.

Dividend Analysis

CVS shares currently yield 2.6%, based on an indicated annual dividend of $2.00 per share. This yield is above the five-year average of 1.5% as well as the five-year average high yield of 1.9%. CVS has been paying a dividend since 1986 and has increased its dividend for each of the last 14 years. Over the last five years, the company’s cash dividend has risen by 27.7% per year on average, ranking it in the top 5% of all U.S.-listed stocks. On December 14, 2016, the company announced that it was raising the quarterly dividend by 17.6%, to $0.50 per share. CVS is currently paying out 34.3% of GAAP earnings, which is near its target payout ratio of 35% by 2018.

The company has been aggressively buying back its shares as part of its commitment to enhance shareholder returns. Since 2012, the company has spent more than $17 billion on share repurchases, lowering its shares outstanding by roughly 17%. During fiscal 2016, which ended on December 31, the company returned $6.3 billion to shareholders in the form of dividends ($1.8 billion) and share repurchases ($4.5 billion).

In fiscal 2016, the company generated free cash flow per share (operating cash flow less capital expenditures) of $7.31, a 35% increase over the prior year. As a percentage of free cash flow, dividend payouts are now 23.1%, which is in line with the five-year average of 23.4%.

Risks

One of the major risks facing the industry is the push for greater regulation and pricing transparency. If the government were to enact pricing caps, PBM acquisition costs would rise, hurting CVS’ returns. In addition, consolidation among suppliers could erode the company’s pricing power.

Margins have been contracting in the wake of the company’s shift in business mix due to the inclusion of Omnicare, the company’s ending of selling wider-margin tobacco products and the loss of the associated non-pharmacy products often purchased on the same shopping trip. •

Bullish Factors

- Large scale allows company to generate some of the highest margins per adjusted claim in the industry
- Demographic shifts should lead to strong pharmaceutical spending over the next several years
- PBMs should benefit from the increase in specialty drug spending as payers look to control costs

Bearish Factors

- Greater-than-expected declines in drug reimbursements would have a material impact on earnings
- Consolidation among drug suppliers could erode CVS’ pricing power
- PBMs are narrowing their pharmacy networks to preserve margins, which could create issues if client members demand more choice

April 2017
## CVS

Addition Alert Date: 4/7/2017  
Price at Alert: NA  
Risk Index: 1.47  
Market Cap (Million): $80,843.5  
Avg Daily Dollar Volume (Million): $568.5  
Primary Sector: Services  
Primary Industry: Retail (Drugs)

CVS, together with its subsidiaries, is an integrated pharmacy health care company. It operates through three segments: pharmacy services, retail/LTC and corporate. The pharmacy services segment provides a range of pharmacy benefit management (PBM) solutions to its clients. The retail/LTC segment includes over 9,700 retail locations (of which nearly 8,000 are its stores that operated a pharmacy and nearly 1,700 were its pharmacies located within Target stores), its online retail pharmacy websites, CVS.com, Navarro.com and Onofre.com.br, 38 onsite pharmacy stores, its long-term care pharmacy operations and its retail health care clinics.

| Indicated Annual Dividend: | $2.00 |
| Latest Dividend Increase: (Date) | Dec 14, 2016 |
| Latest Dividend Increase: (%) | 17.6 |
| Dividend Yield: Current | 2.6% |
| Dividend Yield: Year/Avg (High-Low) | 1.5% (1.9% - 1.3%) |
| Dividend Paid Since: | 1988 |
| Number of Years of Div Increases: | 14 |
| Direct Invest Option: | Yes |
| DRIP Plan: | Yes |
| Declared | Ex-Div Date | Payable | Amount |
| Mar 2, 2017 | Apr 19, 2017 | May 1, 2017 | $0.5000 |
| Dec 14, 2016 | Jan 20, 2017 | Feb 2, 2017 | $0.5000 |
| Sep 22, 2016 | Oct 20, 2016 | Nov 3, 2016 | $0.4250 |
| Jul 6, 2016 | Jul 19, 2016 | Aug 1, 2016 | $0.4250 |
| Mar 2, 2016 | Apr 20, 2016 | May 2, 2016 | $0.4250 |
| Dec 16, 2015 | Jan 20, 2016 | Feb 2, 2016 | $0.4250 |

| Stock Gain | Rel Strth Index | Rel Strth Rank |
| 4 Week | (4%) | 0.97 | 27% |
| 13 Week | (3%) | 0.93 | 39% |
| 26 Week | (11%) | 0.82 | 27% |
| 52 Week | (25%) | 0.65 | 20% |

| Growth | TTM | 3 Year | 5 Year |
| Dividends | 21.4% | 23.6% | 27.7% |
| Sales | 15.8% | 11.9% | 10.6% |
| Net Income | 1.0% | 4.1% | 0.9% |
| EPS Basic | 5.7% | 9.3% | 13.8% |
| EPS Dil Cont | 6.1% | 9.3% | 13.6% |

| Est Surprise | EPS | % Surp | SUE Score |
| Feb 9, 2017 | $1.71 | 2.5% | 4.20 |
| Nov 8, 2016 | $1.64 | 4.6% | 8.00 |

| EPS Estimates | Quarterly | Annual | Annual |
| # of Estimates | 3/2017 | 12/2017 | 12/2018 |
| Current | 21 | 22 | |
| Month Ago | $1.10 | $0.86 | $0.38 |
| # Rev Up | 0 | 1 | 1 |
| # Rev Down | 1 | 0 | 2 |
| Three Mos. Ago | $1.11 | $0.86 | $0.46 |
| Year/Year Chg | 21.0% | 19.6% | 8.8% |

| TTM | $1.59 | $1.43 | $0.87 | $1.04 | $4.93 |
| Year Ago | $1.35 | $1.10 | $1.12 | $0.84 | $4.65 |

| Sales/Sh (Qtr) | 12/2016 | 9/2016 | 6/2016 | 3/2016 | Total |
| TTM | $43.21 | $41.77 | $40.79 | $39.57 | $165.34 |
| Year Ago | $37.20 | $34.69 | $33.03 | $31.77 | $135.17 |

Sources: AAI, Stock Investor Pro, Thomson Reuters and IB/ES/S

$77.87 ($106.67 - $69.30)
Eastman Chemical Co. (EMN)

Eastman Chemical Co. was originally founded in 1920 to produce chemicals for Eastman Kodak (KODK). Since then, the company has evolved into a global producer of specialty chemicals. Eastman’s products have a wide variety of end uses and the company ranks either number one or two in terms of market share for the markets that it serves. Significant revenues are realized in North America, Asia Pacific, Europe, the Middle East and Africa.

Eastman has four business reporting segments: additives & functional products (33% of 2016 revenues), chemical intermediates (28% of revenues), advanced materials (27% of revenues) and fibers (11% of revenues). The additives and functional products segment manufactures chemicals for a variety of end uses including tires, coatings, consumables and feed additives. The chemical intermediates segment manufactures products used for industrial chemicals and processing, building and construction, health and wellness, and agrochemicals. The advanced materials segment produces specialty plastics, interlayers and films. The fibers segment produces acetate products.

Why Own EMN?

Eastman has sought growth through both existing products and strategic acquisitions. The most notable purchase in recent years was the $2.8 billion acquisition of Taminco in 2014. Taminco gave Eastman Chemical access to markets it previously had little presence in, such as agriculture, animal nutrition, water treatment, and oil and gas end markets. No acquisitions have been made recently because of prevailing valuations. During the company’s fourth-quarter conference call, CEO Mark Costa described the current acquisition multiples as being “way outside of the range” he believes would provide an attractive rate of return.

Sales have grown at a 4.6% annualized pace over the past five years. The company’s streak of annual sales growth was interrupted in 2016 with a 6.6% decline. Lower oil prices, lower selling prices, weak economic conditions and the stronger dollar all weighed on the company’s sales. Eastman’s executives view the downward pressures as short-term in nature and do not believe that the long-term outlook has changed. They further think growth in high-margin products as well as in niche products will help revenues grow this year.

Despite the sluggish environment, operating profit margins remain within the company’s historical range and above the chemical manufacturing industry median. The company’s 19.5% return on equity is also far above that of its industry peers.

Earnings per share grew slightly last year. Costa expects growth to accelerate this year with adjusted earnings of between 8% and 12%. Cost reductions combined with growth in certain end markets and in specialty products are forecast to be the key drivers.

Shares trade at a price-earnings ratio of 14.0. This valuation is close to the stock’s five-year average of 13.8. Eastman’s current price-earnings ratio ranks approximately within the bottom 12% of all S&P 500 stocks and within the bottom quartile of all stocks within our Stock Investor Pro fundamental stock screening and research database.

Dividend Analysis

Eastman has raised its dividend at a 13.2% annualized rate over the past five years. This past December, the company announced a 10.9% increase. Though still in the double-digit range, it was the smallest hike since 2011. This made 2017 the seventh consecutive year with an increase.

Eastman has both the financial ability and the stated intent to keep growing its dividend. Its payout ratios remain low on an absolute basis, at 31.8% of earnings and 35.5% of cash flow. The company has routinely been cash flow positive. Plus, Eastman lists its priorities for free cash flow as paying “an increasing dividend,” paying down debt and accelerating its share repurchases.

Shares yield 2.5%. This is above the stock’s five-year average range of 1.8% to 2.5%, implying an attractive valuation.

Risks

Eastman reported lower selling volume and prices for various products in all four of its segments last year. Changes in raw material and energy costs particularly created headwinds for copolysters and methanol. Acetate tow prices and volume were hurt by weak demand in China.

The majority of Eastman’s revenues are realized in foreign countries, exposing the company to both economic and currency risk. The stronger dollar has adversely affected revenues in the various segments.

The company’s products are often used in the production and manufacture of other products. As a result, Eastman lacks control over its customers’ products and end-market demand.

Bullish Factors

- The current valuation is cheap on both an absolute basis and relative to the company’s historical range
- More profitable than industry peers and free cash flow used for double-digit percentage dividend growth
- Sells to a variety of markets, and is a leader in many of the product categories it targets

Bearish Factors

- Sales prices and volumes declined last year for product lines hurt by low energy and low raw material prices
- Majority of revenues realized outside of North America, exposing company to global and national (e.g., China) economic and currency risks
- Lacks the ability to influence end-market demand for its products
Eastman Chemical Company is a global specialty chemical company that produces a broad range of advanced materials, chemicals and fibers. Eastman's businesses are divided into four reporting segments: additives & functional products (coatings, resin, tire industry, animal nutrition and crop protection), advanced materials (specialty plastics, interlayers and films), chemical intermediates (chemical intermediates, amines, specialty fluids and plasticizers) and fibers (acetate products). The company operates globally, selling to customers in more than 100 countries.

Eastman's stated objective is to be an outperforming specialty chemical company with consistent earnings growth and strong cash flow.
Eaton Corporation (ETN)

Eaton is a global manufacturer of products that help to manage electrical, hydraulic and mechanical power.

Eaton’s electrical products segment (34% of full-year 2016 sales; 45% of operating profit) manufactures items such as electrical and industrial components, residential products, wiring devices, circuit protection and power distribution assemblies. Its electrical systems and services segment (31% of sales; 25% of profit) serves the electrical power demands of commercial, governmental and residential markets. Its hydraulics segment (11% of sales; 5% of profit) makes items such as pumps, cylinders, valves and hydraulic power units. The aerospace segment (9% of sales; 12% of profit) makes systems and applications for commercial and military aircraft. Its vehicle segment (15% of sales; 13% of profit) makes truck transmissions, antilock braking systems and engine management systems.

Eaton is a global company, with around half of its sales in foreign markets, including around 24% tied to emerging markets. It has reincorporated in Ireland to minimize corporate taxes.

Why Own ETN?

Eaton is a power management company that has its pulse on both mechanical and electrical power management. For the fourth quarter of 2016, Eaton reported operating earnings of $1.12 per share, above the I/B/E/S consensus estimate. During its fourth-quarter 2016 conference call, the company admitted that this is a difficult market environment and that it is still experiencing weakness in its end markets but anticipates improvement in 2017 over 2016.

Eaton spent $211 million on restructuring costs during 2016; each segment except aerospace is undergoing significant restructuring. The restructuring will allow the company to be more lean and focused on efficiency. Heading into 2017, Eaton expects flat revenue, but continues to see margin improvement in each of its business segments due to restructuring and cost-cutting initiatives. Orders have begun to pick up in hydraulics, a segment that has lagged over the last several years.

Sales have increased at an annualized rate of 4.2% over the last five years, while net income has expanded 7.3% on average and diluted earnings from continuing operations have grown 1.3% on average over the same period.

Eaton’s restructuring plan began in the third quarter of 2015. Eaton expects the restructuring to cost $440 million (from 2015 to 2017) with estimated total benefits of $518 million. The company expects that its restructuring efforts will deliver $155 million of incremental profit in 2017 over 2016, and $175 million in incremental profit in 2018 over 2017. Despite a difficult operating environment, Eaton anticipates full-year 2017 operating earnings per share to be between $4.30 and $4.60, a 5% increase in operating earnings per share on flat revenue.

Dividend Analysis

Eaton has a history of returning excess cash to its shareholders in the form of dividends. The company has paid a dividend every year since 1923. It has increased its annual payout for the last eight consecutive years, holding its annual dividend steady during 2008 and 2009. Dividends have expanded at a 10.9% average annual rate over the last five fiscal years. Eaton’s last dividend increase was 5.3%, declared on February 22, 2017, after increasing its payment 3.6% in 2016. The company’s current dividend yield of 3.2% is in line with its five-year average yield.

Eaton has an acceptable current earnings payout ratio of 53.9%, above the five-year average of 48.7%. The pre-dividend free-cash-flow payout ratio is 50.0%, which is below the five-year average of 55.4%.

During 2016, Eaton spent $730 million on share repurchases, buying back roughly 2.6% of its outstanding shares since the beginning 2016. Eaton expects to repurchase $750 million of its stock during 2017 and return 6% of its market cap to shareholders in 2017 via dividends and share repurchases.

Risks

The weak global economy continues to be a headwind, along with currency exchange rates. Due to global economic weakness, the company expects organic revenue to be flat in 2017 (although this is an improvement over 2016). Eaton’s operations are involved with the oil and gas industry, as well as the global agriculture industry, both of which are experiencing significant weakness.

Eaton expects markets to remain “sluggish” for the rest of 2017, despite signs of improvement in some of its segments. In its fourth-quarter earnings conference call Eaton reiterated that it is still seeing weakness from its end markets tied to oil and gas and large industrial projects.

While the company expects significant incremental profit from its restructuring, there is always the risk that restructuring may not work out as planned. Additionally, significant restructuring can make the company’s comparability year over year difficult.

Bullish Factors

- Significant free cash flow used to boost dividend, repurchase shares and make strategic acquisitions
- Forward price-earnings valuations are reasonable relative to the industry median
- Aggressively reducing costs to maintain leading market position

Bearish Factors

- Diversified, but can suffer during economic slowdown
- Foreign exchange remains a headwind
- Expects flat revenue in 2017
Eaton is a diversified power management company. It is engaged in the manufacturing of electrical components and systems for power quality, distribution and control; hydraulics components, systems and services for industrial and mobile equipment; aerospace, fuel, and pneumatic systems for commercial and military use; and truck and automotive drivetrain and powertrain systems for performance, fuel economy and safety. It has five segments: electrical products, electrical systems and services, hydraulics, aerospace, and vehicle. In 2012, Eaton acquired Cooper Industries plc and relocated to Ireland.
Occidental Petroleum (OXY)

Occidental Petroleum was founded in 1920 and is one of the largest oil and gas companies in the United States. It operates in three business segments: oil and gas (63% of 2016 revenue), chemical (37% of revenue) and midstream and marketing (7% of revenue).

Occidental is the largest producer of oil in the Permian Basin (Texas and New Mexico), one of the largest and most active oil basins in the U.S. The company also produces oil in the Middle East (UAB, Oman and Qatar) and Latin America (Colombia). Chemical segment Oxychem focuses on being a low-cost producer of chlorovinyls. The midstream business transports and stores energy products.

Occidental prefers to hold large, long-lived legacy oil and gas assets, which is why it is focused on the Permian Basin. Total Permian oil production grew 13% during 2016 compared to OXY’s overall production growth of 7%.

With lower energy prices, Occidental reduced its capital and operating costs and is optimizing its portfolio to focus on its core assets in the Permian Basin and Middle East. It is favoring production of oil fields over natural gas fields. It has divested assets with lower free cash flow and higher country risk. The company will focus its Middle East business in Abu Dhabi, Qatar and Oman.

Why Own OXY?

Occidental is a financially sound company with a reasonable dividend valuation. Debt has grown, but remains at a manageable level, with a liabilities-to-assets ratio of 50.1%. Efforts to lower production costs indicate that operating cash flow can cover dividend outlays and growth capital programs with oil prices around $60 per barrel. OXY is targeting long-term oil and gas production growth of 5% to 8% per year.

Occidental does not have a meaningful trailing or forward price-earnings ratio due to negative earnings related to lower oil prices. The firm is expected to return to profitability in 2017, and it is generating positive cash flow from operations.

Risks

Oil is a commodity and its prices have historically been volatile, with significant price swings that the company has no control over. The impact of these price swings is reflected in the changing consensus earnings estimates for Occidental. Revisions by many analysts have lowered the fiscal-year 2017 I/B/E/S consensus earnings forecast from $1.38 per share three months ago to $1.13 per share currently. OXY is expected to earn $2.03 per share in 2018 and $2.65 in 2019, but this is highly dependent on energy prices.

Occidental has historically spent heavily on capital investment but has been slashing such costs in recent years. Though this spending is necessary to drive future earnings growth, it has resulted in years where free cash flow is low or negative.

Occidental’s reliance on the Permian Basin leaves it more concentrated than the other major integrated oil companies. Plus, its foreign assets are located in the politically unstable areas of Colombia, the Middle East and North Africa. For example, pipeline disruptions from Colombian guerrilla groups are impacting sales volume.

Dividend Analysis

Occidental is the rare company that has offered both a high relative yield and a historically high dividend growth rate. Over the past five years, the annual dividend growth rate has averaged 10.4%. Occidental currently yields 4.7%, above its five-year average yield of 3.5%. The company raised its quarterly dividend by 1.3% in July 2016, a rarity for oil firms in the past year. The company has raised its dividend each year for the last 14 years. Dividend growth has slowed as oil and natural gas prices play a key role in capital expenditure and the dividend policy. Capital spending has declined with lower oil prices, but the company expects oil and gas production volume to increase. Capital spending will likely tick up slightly in 2017 ($3.3 billion to $3.8 billion, versus $3.0 billion in 2016), but more projects are moving into production.

Occidental ranks dividends as its second-highest cash flow priority, behind only maintenance but ahead of share repurchases, capital growth and acquisitions. Occidental says that it will be able to fund both its capital expenditures and its dividend out of operating cash flow with oil at around $60 per barrel. OXY makes heavy use of horizontal drilling and has been emphasizing drilling locations with lower breakeven levels.

Bullish Factors

- Largest producer in the Permian Basin, one of the largest and most active oil basins in the U.S.
- Financially sound with a strong balance sheet
- Committed to paying dividend ahead of capital growth, share repurchases and acquisitions

Bearish Factors

- Low oil prices have hurt near-term profitability and cash flow
- Capital expenditures required to sustain and grow oil production results in negative free cash flow at times of low energy prices
- Profitability determined by price of oil and gas over which the company has no control

During fiscal-year 2016, Occidental generated cash flows from operations of approximately $3.38 billion. OXY notes that a dollar change in the price of oil impacts the annual operating cash flow by around $100 million. OXY expects free cash flow to increase by $0.95 billion to $1.0 billion during 2017. Permian resources are expected to generate free cash flow in 2018. OXY ended the quarter with $2.2 billion in cash.
OXY

Addition Alert Date: 1/9/2015
Price at Alert: $77.54  
Risk Index: 1.85
Market Cap (Million): $49,139.5
Avg Daily Dollar Volume (Million): $346.0
Primary Sector: Energy
Primary Industry: Oil & Gas - Integrated

Occidental Petroleum Corp. is an oil and gas exploration and production company with operations in the United States, Middle East/North Africa and Latin America. The company operates in three segments: oil and gas, chemical, and midstream. The oil and gas segment explores for, develops and produces oil and natural gas. The chemical segment manufactures and markets chlor-alkali products. The midstream segment gathers, processes, transports, stores, purchases and markets oil, natural gas and power. It also trades around its assets, including transportation and storage capacity, and trades oil, gas and other commodities.

Indicated Annual Dividend: $3.04
Latest Dividend Increase: Date: Jul 14, 2016
Latest Dividend Increase: %: 1.3%
Dividend Yield: Current: 3.5%
Dividend Yield: 5-Year Avg (High-Low): 3.5% (4.1% - 3%)
Dividend Paid Since: 1975
Number of Years of Div Increases: 14
Direct Invest Option: No
DRIP Plan: No

Declared Ex-Div Date Payable Amount
Feb 16, 2017 Mar 8, 2017 Apr 14, 2017 $0.7600
Oct 6, 2016 Dec 7, 2016 Jan 13, 2017 $0.7600
Jul 14, 2016 Sep 7, 2016 Oct 14, 2016 $0.7600
Apr 29, 2016 Jun 8, 2016 Jul 15, 2016 $0.7500
Feb 18, 2016 Mar 8, 2016 Apr 15, 2016 $0.7500
Oct 8, 2015 Dec 8, 2015 Jan 15, 2016 $0.7500

Growth TTM 3 Year 5 Year
Dividend 1.7% 5.7% 10.4%
Sales (19.1%) (20.5%) (15.8%)
Net Income 92.7% (28.0%) (15.8%)
EPS Basic 92.7% (28.1%) (15.9%)
EPS Dil Coll 87.7% (30.3%) (16.7%)

Est Surprise EPS % Surp SUE Score
Feb 9, 2017 ($0.13) (441.7%) (2.60)
Nov 1, 2016 ($0.15) (38.9%) (0.50)

EPS Estimates Quarterly Annual Annual
# of Estimates 18 24 21
Current $0.16 $1.13 $2.03
Month Ago $0.17 $1.13 $2.03
Rev Up 3 2 7 3
Rev Down 7 8 4
Three Mos. Ago $0.20 $1.38 $2.07
Year/Year Chg 33.9% (188.4%) 79.1%

TTM ($0.35) ($0.31) ($0.18) ($0.47) ($1.31)
Year Ago ($3.21) ($3.41) $0.24 ($0.28) ($10.67)

Sales/Sh (Qtr) 12/2016 9/2016 6/2016 3/2016 Total
TTM $3.69 $3.50 $3.35 $2.81 $13.35
Year Ago $3.72 $4.12 $4.56 $4.05 $16.45

Sources: AII Stock Investor Pro, Thomson Reuters and i/B/E/S.

Dividend Yield (%): Avg 4.7% 4.4 4.0 3.3 3.0 2.5
Dividend Yield (%): High 5.2 4.7 4.0 3.5 3.1
Dividend Yield (%): Low 3.8 3.5 2.9 2.7 2.1
Price/Earnings nmf nmf nmf nmf 13.8 18.2
Price/Earnings (Industry) 11.0 12.1 14.7 18.4 18.7 17.8
Price/Book Value 2.3 2.4 2.3 1.9 1.6 1.7
Price/Sales 4.8 5.1 4.5 3.5 3.4 3.5

Payout Ratio: EPS (%) nmf nmf nmf 365.2 34.9 38.1
Payout Ratio: FCFEPS (%) nmf nmf nmf 498.8 42.8 130.4
Gross Margin (%) 49.1 49.1 53.9 85.0 68.0 67.8
Operating Margin (%) (17.2) (17.2) (76.5) (6.2) 33.1 31.1
Operating Margin (%) (Ind) (14.0) (17.9) (40.8) 12.6 12.4 10.9
Net Margin (%) (5.6) (6.5) (62.1) 3.2 29.0 22.7
ROE (%) (2.5) (2.5) (26.4) 1.6 14.2 11.8
ROE (%) (Industry) (5.4) (9.9) (8.8) 10.4 9.3 9.7
ROA (%) (1.4) (1.3) (15.7) 1.0 8.8 7.4
Current Ratio 1.3 1.3 1.4 1.7 1.3 1.3
Liabilities to Assets (%) 50.1 50.1 43.9 37.9 37.9 37.7
Liab to Assets (%) (Ind) 46.8 42.7 53.8 52.6 46.0 50.6
Asset Turnover 0.2 0.2 0.3 0.3 0.3 0.3

Sales ($M) 10,196 10,196 12,598 19,442 20,277 20,180
Gross Income ($M) 5,007 5,007 6,794 12,639 13,780 13,650
Depreciation & Amort. ($M) 4,268 4,268 4,544 4,261 4,203 3,585
Unusual/Extra ($M) 825 825 10,239 7,379 621 3,461
Operating Income ($M) (1,755) (1,755) (9,638) (1,204) 6,708 6,279
Interest Expense ($M) 292 292 147 77 132 154
Earnings before Interest and Taxes ($M) (1,845) (1,845) (9,884) 1,224 7,751 6,125
Net Income ($M) (574) (574) (7,929) 616 5,880 4,590

Operating Cash Flow ($M) 3,383 3,383 3,351 11,068 12,778 11,299
Investing Cash Flow ($M) (4,742) (4,742) (5,423) (8,470) (8,644) (12,642)
Financing Cash Flow ($M) 391 391 1,484 (2,202) (2,933) (846)
Capital Expenditures ($M) 4,761 4,761 5,381 10,817 7,963 9,958
Net Cash Flow ($M) (998) (968) (588) 396 1,801 (2,189)
EPS Basic ($) (0.75) (0.75) (0.23) 0.79 73.3 5.67
EPS Diluted Coll ($) (1.31) (1.31) (10.64) (0.18) 6.12 4.72
EPS DC Year/Year Chg (%) 87.7 (87.7) 5,682.6 (103.0) 29.6 (42.1)
Dividends/Share ($) 3.02 3.02 2.97 2.88 2.56 2.16
Dividend Year/Year Chg (%) 1.7 1.7 3.1 12.5 18.5 17.4
Free Cash Flow/Share ($) (1.80) (1.80) (2.65) 0.58 5.99 1.66

Goodwill/Intangibles ($M) 0 0 0 0 0 0
Total Assets ($M) 43,109 43,109 43,409 56,259 69,443 64,210
Long-Term Debt ($M) 9,819 9,819 6,855 6,838 6,939 7,023
Total Liabilities ($M) 21,612 21,612 19,050 21,300 26,317 24,194
Book Value/Share ($) 28.13 28.14 31.81 44.76 53.63 49.45
Avg Shares Outst/g (M) 764 764 766 781 804 809

Determining Your Portfolio's Expense Ratio

New subscribers often ask how much they should invest in each stock when building their DI portfolio. Understanding the impact of trading costs, average position size and frequency of trading on your portfolio's actual return is a critical consideration to keep in mind. Looking at how much you invest and its impact on your portfolio expense ratio can help you make an informed decision.

Desired Expense Ratio
If you are using an online discount broker such as Scottrade ($6.95 per trade, $13.90 round trip), buying and selling all 24 DI holdings would cost you $333.60 ($13.90 × 24). If you invest $2,000 per stock, this would be equal to an expense ratio of 0.70% ($333.60 ÷ $48,000). The “round-trip” cost is used with the assumption that you will eventually sell your shares.

If you hold only 12 stocks (the minimum recommended for a portfolio of DI stocks) and invest $4,000 in each holding, you would pay $166.80 in commissions ($13.90 × 12 stocks), for an expense ratio of 0.35% ($166.80 ÷ $48,000). A trade off exists when you reduce the number of stocks you buy (cost goes down but risk goes up because of less diversification).

Popular discount brokers such as Scottrade, Fidelity, Charles Schwab, TD Ameritrade and E*Trade offer competitive commission rates. AAII members can rate their brokers and see the year-end results on AAII.com in the Online Discount Broker Survey (www.aaii.com/brokersurvey). All the aforementioned brokers have recently lowered their commissions.

For a benchmark to compare costs against, you could look at mutual funds. A majority of DI holdings are large-capitalization stocks; according to AAII's Guide to the Top Mutual Funds (February 2017 AAII Journal), the average large-cap stock fund's expense ratio is 0.89%. Using the same cost as above, if you are using a broker that charges $6.95 per trade ($13.90 round trip) and want to create a DI portfolio with the minimum suggested 12 stocks, you are looking at a total commission of $166.80. Dividing $166.80 by the target expense ratio of 0.89% gives a total investment amount of $18,741, or $1,561 invested in each of the 12 stocks.

When considering these examples, it's important to remember that mutual funds calculate their expense ratios on an annual basis to allow comparability across funds and help measure how it impacted the realized return. As the value of your fund shares increase, so does the absolute dollar amount you will pay in fees. This differs from purchasing individual stocks for a portfolio because when you buy and sell, you only pay the commission.

Overall, when deciding how much money to commit to your DI portfolio, keep in mind that buying stocks in small dollar amounts will lead to higher transaction costs as a percentage of your portfolio’s value. These higher proportionate costs will reduce the return you realize.

Factoring in Portfolio Turnover
Part of the DI approach is to minimize portfolio turnover. Turnover is important because the more frequently you trade, the more your realized return will be reduced by brokerage fees, the impact of the bid-ask spread and the possibility of higher taxes on realized short-term versus long-term capital gains. Plus, studies have shown that active trading leads to worse performance (e.g., see “Trading More Frequently Leads to Worse Returns” in the November 2014 AAII Journal).

Higher portfolio turnover raises portfolio ownership costs through direct and indirect transaction costs as well as creating taxable capital gains on shares held in a taxable account. Portfolio turnover is measured by the percentage of your total portfolio value that is traded over a particular period. For example, an annual portfolio turnover of 25% means that a quarter of the value of your portfolio was traded over the year. A high turnover rate, of 200% for example, indicates that you have turned over twice the value of your portfolio in a year, holding your securities for just six months on average. This increases the likelihood of paying short-term taxable gains at the higher marginal tax rate.

Looking at the current holdings of the DI tracking portfolio, the 12-month turnover rate is 28%, for an average holding period of roughly three and a half years (1 ÷ 0.28). Since inception, the annual 12-month rolling portfolio turnover rate of the DI portfolio has averaged 24%. The portfolio turnover was highest in February 2017 at 32%. The last time it was this high was October 2015, when turnover reached 31%. With a 24-stock portfolio, a turnover rate of 32% is an average of seven portfolio additions and seven portfolio deletions per year. However, the DI approach reinvests dividend income into underweighted portfolio holdings. The DI tracking portfolio has averaged around three such additional dividend reinvestment purchases per year, pushing the overall average to 10 purchases and seven deletions per year.

With an average of 10 purchases per year and seven deletions (17 trades total), you’re looking at $118.15 per year in transaction costs (at $6.95 per trade). To reach a target expense ratio of 0.50% in any given year, you’d have to have roughly $23,630 invested in the portfolio ($118.15 ÷ 0.005). This would mean $984 invested in each of the 24 stocks.

If you choose to not follow the active reinvestment approach implemented in the DI tracking portfolio by selectively choosing which holdings to reinvest excess cash into, one option is to enroll in a dividend reinvestment program. While most companies allow you to do this directly through the firm, many brokerages offer the same service. With Charles Schwab, E*Trade, Fidelity, TD Ameritrade and Vanguard, you can reinvest your dividend payments at no cost. Scottrade has a “flexible reinvestment program” which allows dividend reinvestment, but has some stipulations.