DSR PREMIUM NEWSLETTER

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This is your site and your exclusive newsletter. Please, feel free to share any ideas, opinions, comments, or suggestions with us via email at dividendustries@gmail.com.

DECEMBER 29TH, 2023

Dear DSR member,

It is with great pleasure that we present our weekly premium newsletter which is an important component of your subscription to Dividend Stocks Rock.

You may benefit from viewing our video explaining the differences between the Buy List, our ratings, and our portfolio models. You can retrieve this information in the Videos section of the website.

Referral

Feel free to share our ideas with your friends or associates who may benefit from this information. **We would personally consider any referrals you make on our behalf to be the ultimate compliment for our efforts.**

DIVIDEND STOCKS ROCK
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INVESTMENT THEMES FOR 2024

Before I tell you what I found in my crystal ball for 2024, let's keep in mind this quote:

"… the big trends mostly right will not always lead to the outcome that you anticipate."

~ *Mackenzie 2024 Market Outlook*

A quick word of warning before we start: **while adjusting for the ever-evolving market, one should only tweak his/her portfolio and not completely change it.** The key remains to be loyal to your strategy.

To put it in simple terms: stay invested.

RECESSION – ARE WE THERE YET?

This is a tale of two economies. On one side, we have a U.S. resilient economy with consumers who want more. On the other side, we have Canadians starting to lose their breath as they can't keep up with this spending marathon. One thing Americans have on their side is their long-term, fixed-rate mortgages, while most Canadians take 5 years or less for their mortgage contract.

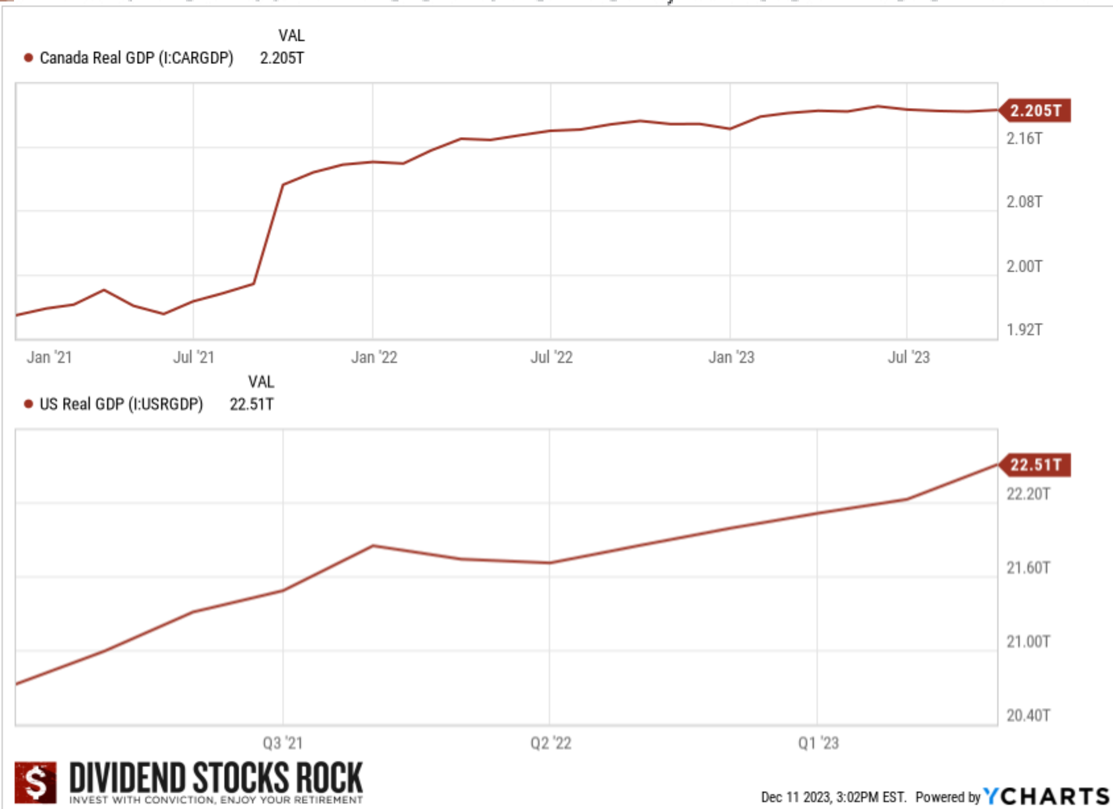
But let's not forget that while the S&P 500 was up double-digits this year, only a handful of stocks contributed to this success story. The magnificent 7 (Apple, Microsoft, Alphabet, Amazon, Nvidia, Tesla, and Meta) constitutes about a third of the S&P 500 value but is also responsible for about two-thirds of the S&P 500 bull run in 2023 (Mercer Themes & Opportunities 2024).

Last year, I agreed with analysts surveyed by Bloomberg that 2023 was the year of the recession. My message to my DSR members was clear: clean your portfolio, fortify it with strong companies, and brace for impact. While my message was right, I was completely wrong about the recession.

We saw the first signs of a slowdown in Canada in late 2023, but we are far from calling this a recession. Yet. I'm still convinced the economy will suffer from the deadly combination of a high rate of inflation and higher interest rates. Most consumers have completely forgotten what it's like to pay a 7% interest rate on their home's mortgage. It's even harder when your mortgage payment has doubled, and you must pay more for your groceries as well.

While the economy may slowdown in 2024, the job markets seem just fine on both sides of the border. Demographics are on our side as more people retire each year than people join the labor force. We are close to full employment (especially in the U.S.) which should put some pressure on inflation and help the famous "smooth landing" central banks are hoping for.

Recession or not, the current interest rate environment will have many impacts on 2024.


VAL
Canada Real GDP (I:CARGDP) 2.205T
2.205T
2.16T
2.08T
2.00T
1.92T
Jan '21
Jul '21
Jan '22
Jul '22
Jan '23
Jul '23
VAL
US Real GDP (I:USRGDP) 22.51T
22.51T
22.20T
21.60T
21.00T
20.40T
Q3 '21
Q2 '22
Q1 '23
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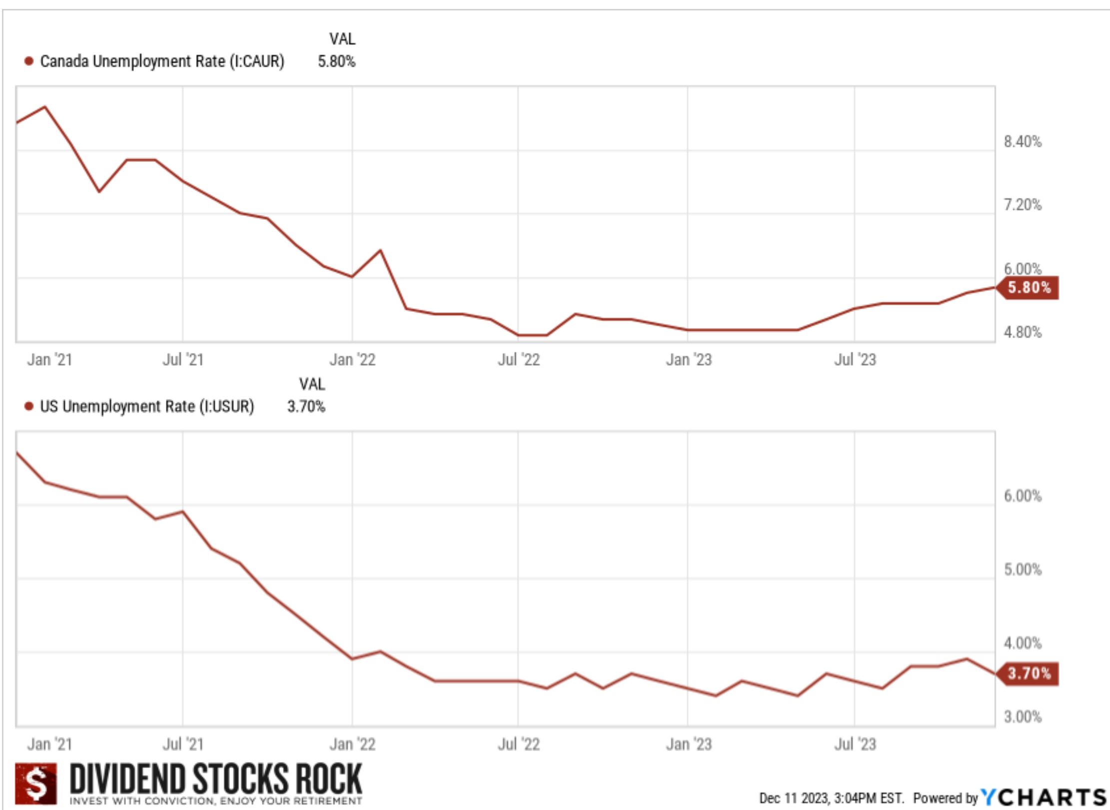
Dec 11 2023, 3:02PM EST. Powered by YCHARTS


VAL
Canada Unemployment Rate (I:CAUR) 5.80%
8.40%
7.20%
6.00%
5.80%
4.80%
Jan '21
Jul '21
Jan '22
Jul '22
Jan '23
Jul '23
VAL
US Unemployment Rate (I:USUR) 3.70%
6.00%
5.00%
4.00%
3.70%
3.00%
Jan '21
Jul '21
Jan '22
Jul '22
Jan '23
Jul '23
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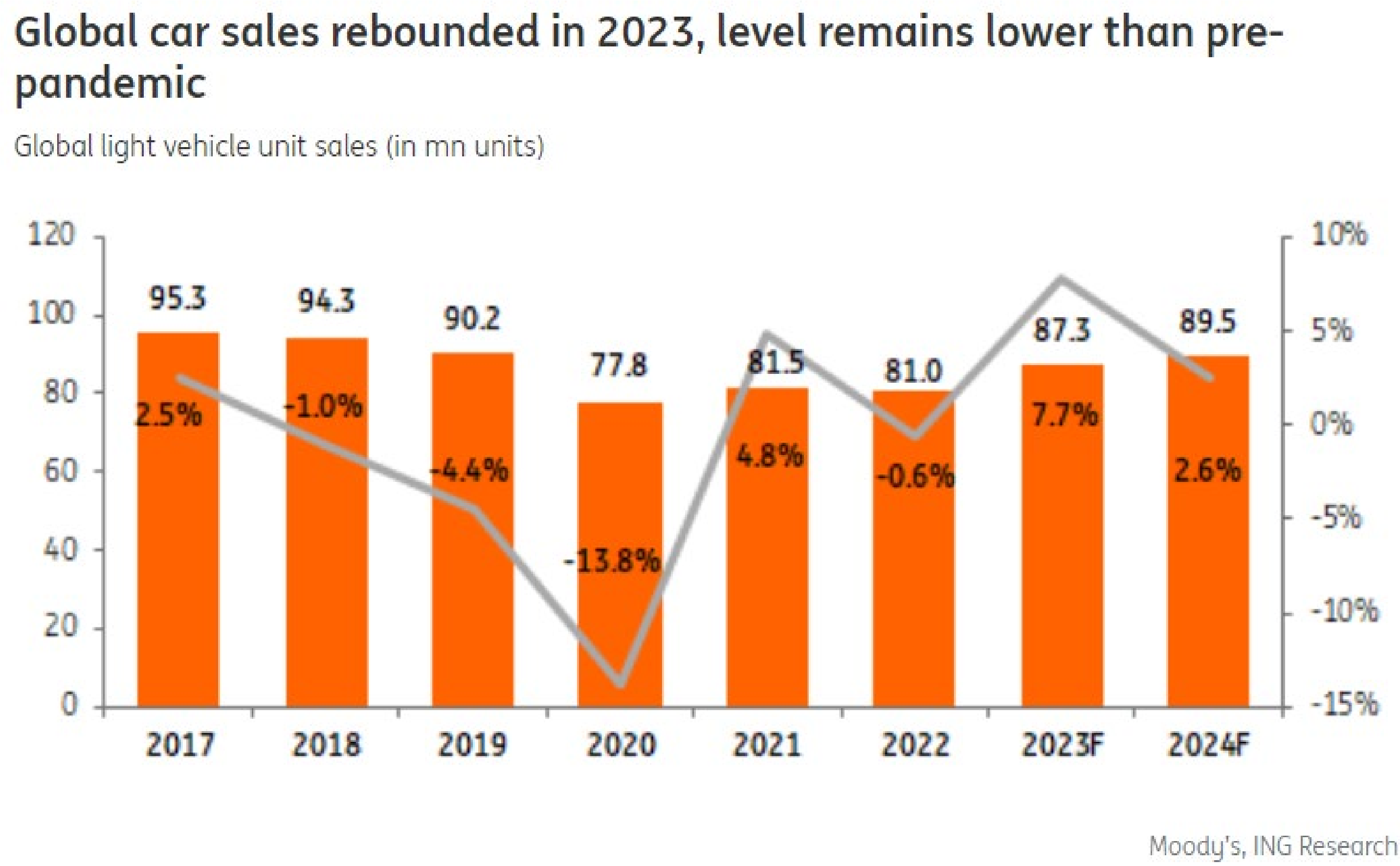
Dec 11 2023, 3:04PM EST. Powered by YCHARTS

Lower earnings expectations

When you review your quarterly earnings using your DSR PRO report in 2024, don't be surprised to see many companies showing weaker earnings. Many industrials and automotive companies will show a slowdown. It's also true for many consumers discretionary companies that they will see consumers keeping their wallets in their pockets. For example, Canadian Tire (CTC.A.TO) reported weaker sales for "discretionary items" while consumers focused on essential purchases. In the U.S. Home Depot (HD) confirmed that consumers aimed at smaller projects in 2023 which affected their sales. Car sales are expected to just barely increase in 2024. The list goes on and on.



Unfortunately, this means that if you hold cyclical companies, they may report a few bad quarters in 2024. Should you jump ship? The short answer is "no", but we will discuss that issue further later in this newsletter.

Zombie companies

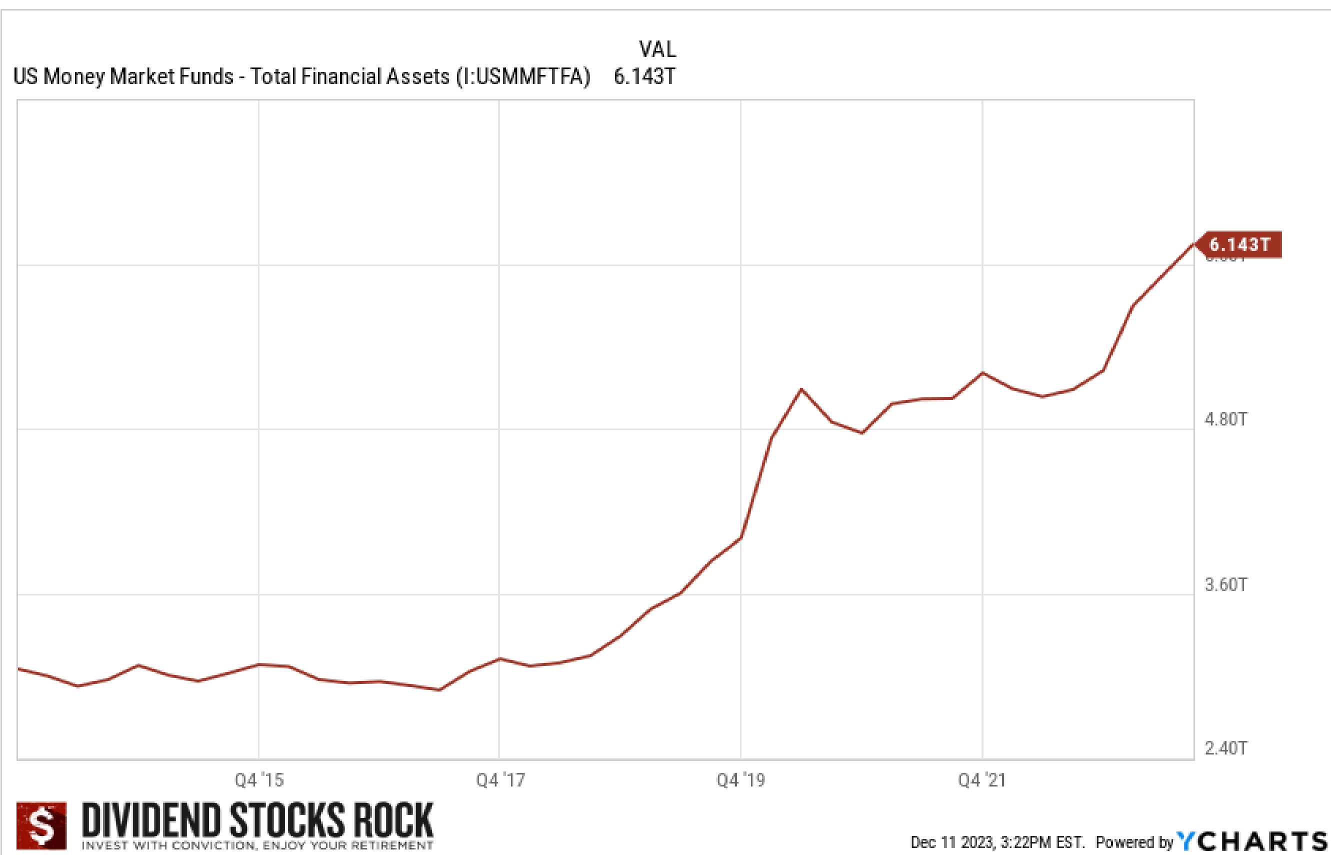
Bloomberg tracks the amount of "zombie companies" on May 22nd of each year. Zombie companies are deemed to be those companies with an interest coverage ratio of <1. In other words, companies relying heavily on leverage to survive. This number usually hovers around 500 pre-COVID-19 but it's now above 700. Once again, we will see companies (or zombies) die in 2024 as pressure from the higher interest rates isn't over. It's not because we hear chatters of rate cuts somewhere in 2024 that we are going back to a "free money era".

Interest rates will continue to be relatively high, and companies will renew their debt accordingly. On top of zombie companies, many capital-intensive businesses (notably telcos, utilities, REITs, and some industrials) will see their interest charges increase once again in 2024. The lagging effect will last throughout the year and beyond.

Brace for impact.

What could happen instead…

I know, I just painted a bleak future for your investments. However, it doesn't mean you should quit and run towards bonds. According to Morningstar, there is at least $6 trillion sitting in cash on the sidelines.



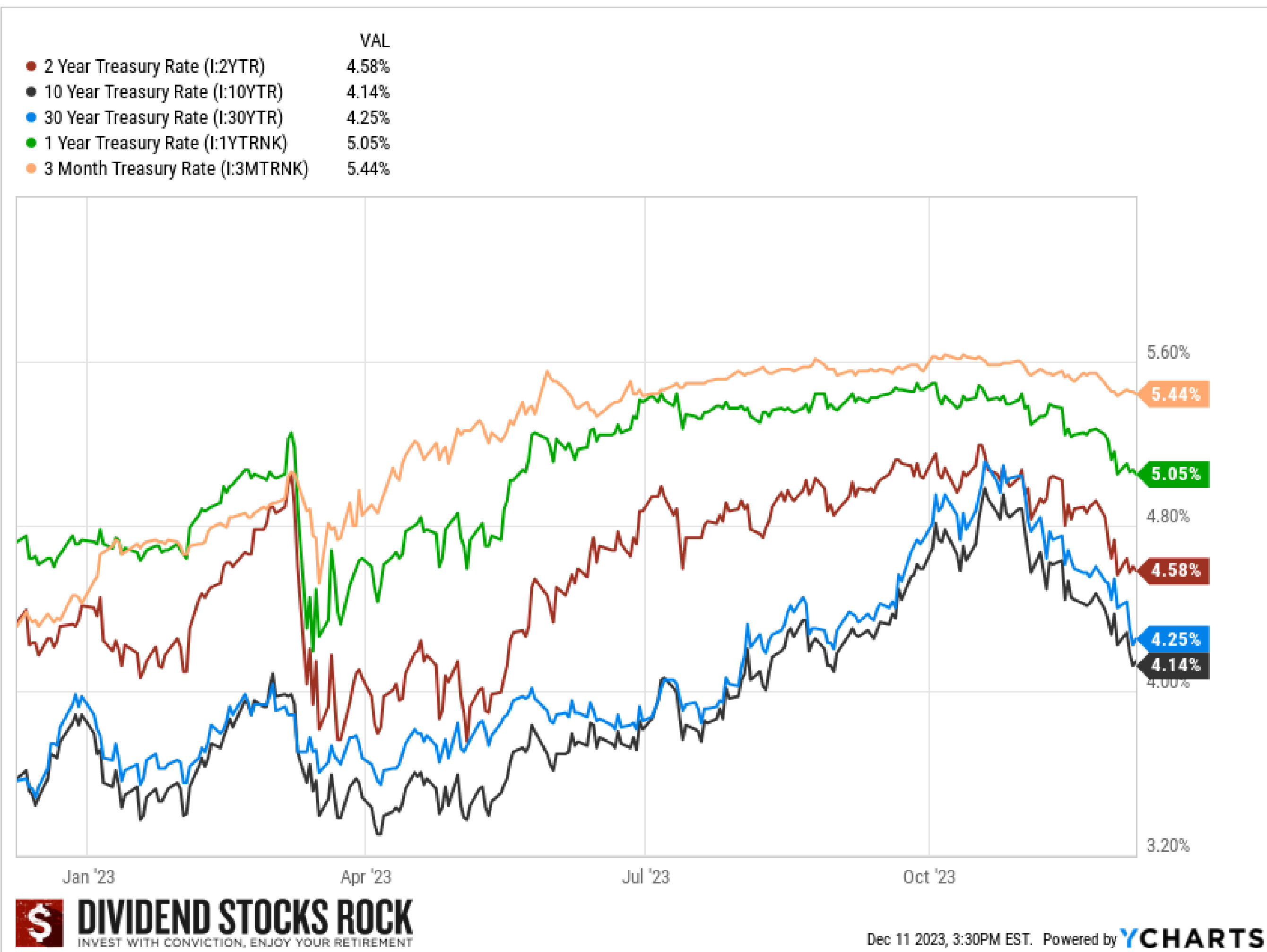
This is the highest level of liquidity we have ever seen in U.S. money market funds. What do you think will happen to the market if we hear Powel say the magic "C" word? Money won't go into bonds, and it won't stay in declining high-interest savings accounts. It will likely go back to the market.

That's one more reason to stay invested and make sure you are confident in your holdings (I have a playbook later for you).

Bond rally?

If you are an income-seeking investor, you might want to load up on bonds. Chances are that short-term bonds will do well in 2024. Many expect rates to decline. As short-terms bonds are directly linked to interest rates, they will start going up in value (as new short-term bonds should offer lower interest rates).

There is less money to be made with long-term bonds as the decline has already started in October of 2023 (see graph below).



The yield curve is inverted (short-term bonds offer higher yields than long-term treasuries). In general, long-term bonds will offer better yields than short-term treasuries. When the yield curve is inverted, it's a sign that the market doesn't believe better days are ahead and rather believes interest rates are about to decline. The message can't be clearer.

I'm not a fan of jumping from one strategy to another (or one asset allocation to another). I would rather keep a consistent allocation and strategy for decades. It's not only easier to apply, but it also gets rid of all doubts and dilemma. Plus, the power of compounding is found in patience.

IS AI THE SOLUTION TO COST SAVINGS?

As I wrote earlier, many companies will continue to suffer from the expected economic slowdown, higher interest charges, etc. What will they do? Record exceptional charges affecting their EPS for… restructuring!

The cost savings plans trend will continue to expand as companies will look for more ways to get leaner and improve their margins. Instead of simply laying off employees, they can also look at other ways to improve their productivity. One way is new and not new at the same time.

Ironically, artificial intelligence (AI) has been around for several decades. The first trace of AI dated from the 50's! However, the past 5 years have been crucial in the development of this technology. I'd suggest the podcast series made by the Wall Street Journal called "Artificial".

The improvements coming from AI are real. However, trying to surf that wave could result in crashing hard on the shore. I guess you remember how the Cannabis trend ended in 2018. Instead, you can invest in companies that will benefit from the wave, no matter what. It's great since there are a few dividend payers among that group!

Chip markers: A classic play with companies like Nvidia and AMD as "obvious" winners. You can bet that other semiconductor companies like TSM, Broadcom or Intel may also benefit from the number of chips required to power AI. Semiconductor equipment providers such as Lam Research or ASML could also see their backlogs increase.

Software enterprises: Companies like Microsoft and Oracle will use AI to increase the power of their software. Other companies such as Accenture may use AI to boost their consulting and strategy services.

Healthcare, Consumer & Industrial markets: Many healthcare companies have already started investing in AI to improve their productivity. Companies like Abbott Laboratories, Medtronic and McKesson are part of that group of innovators.

THE RENEWABLE WILD WEST & INVESTMENT IN INFRASTRUCTURE

It has been quite a rollercoaster for renewables over the past two years. Let me rephrase that: it has been an ever-falling cliff! Those companies rely heavily on debt and also on issuing more shares to fund their projects. On top of that, they are heavily dependent on government investments or subsidies.

Wind energy and headwinds

The wind energy sector is probably the one that has been the most affected as it faces multiple challenges:

Financing costs: Wind farms are complex to setup and require time and money. As interest rates increased, it became quite expensive to set-up wind farms (as opposed to installing solar panels on rooftops!).

Inflation management: Costs of construction exploded due to the number of raw materials required (think big steel structures). Inflation drove those costs through the roof while the business is still struggling to thrive without Government subsidies.

Connectivity cost: In general, it costs more to connect wind farms to the grid. Adding all the costs (financing, construction and connection costs) makes it a less economic energy solution for now.

Solar is easier

Solar panels are amongst the cheapest ways to generate electricity. It is intermittent (similar to wind energy), but it's still more predictable. However, it seems obvious the solution to reduce carbon emissions is a combination of multiple energy sources such as hydro electricity, wind & solar energy along with natural gas and potentially nuclear energy as well.

Like it or not, governments keep spending billions on those projects and this also leads to major infrastructure spending. My favorite utilities for this play are the Brookfield (Renewable and Infrastructure), NextEra Energy (the parent company) and Xcel (a great mix of regulated and green energy).

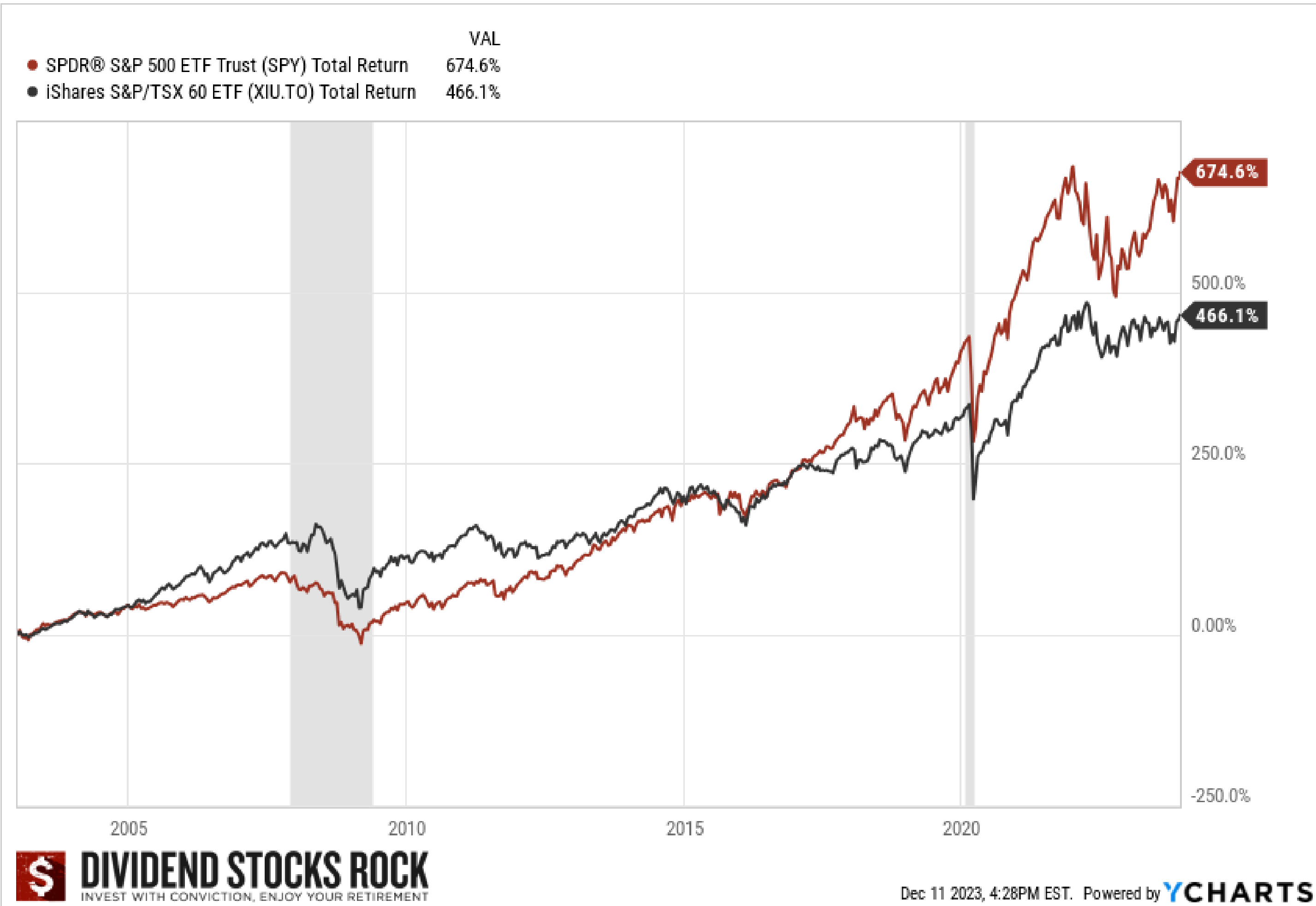
There aren't only utilities where you can invest and benefit from this wave of money.

Alternative asset managers are key players

The biggest problem with such projects is that they don't generate immediate cash flow. Far from it. To invest and manage them, you need to be a specialist in "patient capital". They are known as alternative asset managers. From a portfolio management perspective, investing in alternative assets is a great way to diversify your portfolio. Typically, the investment returns on such investments will not be determined by what is happening in the stock market. You can expect they will generate about 5-7% above inflation over long periods of time. My favorite players in that category are Brookfield (BN or BAM) and Blackstone (BX) which is the largest one.

SHORT-TERM RESULTS – LONG-TERM GOALS?

I started investing in 2003. Chances are you may have started before me. What is the most important lesson you can dig from your experience with Mr. Market? While the short-term view could be cloudy, scary, or simply pitch black, the long-term view often looks like this:



Imagine if I would have stayed on the sidelines for 3 years after the tech bubble crash and 2 years after the World Trade Centre tragedy? Imagine if I had quit during the financial crisis, the European debt crisis, the Brexit crisis or COVID-19? I would have missed a magical 20 years in the market! When I look at this graph, I come to two conclusions:

1. Obviously, staying fully invested is the best solution, always.
2. For several years, the market doesn't give you much. This is where you test your patience, and you focus on your growing dividends to maintain the cap.

PLAYBOOK FOR 2024

The point is not to transform your investing strategy and start from scratch. This section is more about adjusting your portfolio to make sure you are well-invested and that you have seen clearly what is coming. A potential long bear market will impact two different types of investors: those who are invested and those who have cash on the side. Here's a playbook for each of them.

Invested investors (like me!):

1. **Review** your portfolio to ensure you are well-diversified across many sectors
2. **Identify** weaker-rated stocks and make sure you still want to hold them
3. **Trim** overweight positions (Apple and Couche-Tard could be good candidates in my portfolio)
4. **Optimize** your holdings with better-rated stocks using the DSR PRO replacement list
5. **Build** a cash reserve if you are retired and depend on your portfolio to generate income

The cash reserve will be used to supply income in addition to the dividend payments you will receive. I don't intend to build a cash reserve as I'm still in growth mode.

Cash on the side investors (sitting, waiting, wishing…)

1. **Build** a buy list right now
2. **Invest** 33% of your money now
3. **Wait** for another quarter, review earnings, and invest an additional 33%.
4. **Rinse & repeat** for another quarter to fully invest your money over the next 6 to 9 months.

The key with this strategy is to make sure your portfolio thrives no matter if you invest right before a market crash or if we are about to ride another 5 years of bull market. Imagine your worst fear materializes and you invest literally days before a crash starts. Major market crashes are usually violent, and the down trend doesn't last very long. Therefore, you'll be buying the dip 3 months and 6 months down the line. You may not buy at the bottom, but you will surely be averaging down your position with cheaper prices. On the other side, if markets continue to rise, you'll be slowly building a profit cushion with invested money. If you wait, you may wait for years and never get today's price. I'll bet you thought 2017 markets were overvalued and that you would likely have many opportunities to buy stocks at better prices, right?

Wars & Politic tensions

One last sub-topic I didn't address in this newsletter is the ongoing wars and politic tensions that are growing. This will make the news, it will scare the market, and most importantly, it will create tragedy around the world. However, from an investment perspective, it will have a limited long-term impact. It is very sad to say, but humans and companies adapt quickly to a new environment. You can only look at natural gas prices from my previous newsletter covering the energy sector to realize how fast it went back to pre-war level while the Russia-Ukraine war is still raging.

Find quality income investments

No matter what you do with your portfolio, **do not just go for the yield.** Don't get me wrong, it's okay to have higher-yielding stocks in your portfolio. With the right amount of research, you can find companies that won't let you down and keep their generous dividends growing. But that's not all of them. Go for quality and for dividend safety first.

For stocks you are not 100% convinced will do well, you can reduce your exposure and make sure they won't make a hole in your portfolio if they crash and burn. That little piece of advice has saved me several times in the past. By limiting my exposure to "educated guesses" or "sexy ideas", I made sure to preserve most of my capital.

FINAL THOUGHTS

Many factors will have an influence on the market in 2024. However, the best way to start the year remains the same: having a straightforward strategy. In other words,

"*Know what you own and know why you own it.*"

- Peter Lynch

I hope this newsletter has given you some food for thought and that it will help you see things more clearly as we enter the New Year 2024.

Again, I thank you for your trust and may 2024 be filled with joy, health & wealth!

As always, if you have questions or topics, you would like me to discuss, I'm only one email away!

Cheers,

Mike.

RATING CHANGES

This section communicates rating changes on the most popular stocks held at DSR. The changes mentioned below happened during this week upon our latest review.

No rating changes.

COMPANY	SYMBOL	PREVIOUS RATINGS (PRO/DIV)	NEW RATINGS (PRO/DIV)	COMMENT

OVERALL PORTFOLIO PERFORMANCE

Listed Returns are as of December 19th 2023:

Portfolios	Inception Date	Return	Benchmark	Added Value	Annualized Return	1 Y	YTD
CAD 25K	10/31/13	206.30%	130.86%	75.43%	11.57%	8.02%	14.90%
USD 25K	10/31/13	173.49%	187.68%	-14.19%	10.35%	2.67%	8.07%
CAD 100K	10/31/13	135.47%	130.86%	4.61%	8.74%	5.99%	12.13%
USD 100K	10/31/13	223.62%	187.68%	35.94%	12.18%	12.31%	17.39%
USD 500K	05/31/14	116.06%	155.26%	-39.20%	8.39%	5.70%	10.08%
CAD 500K	05/31/14	123.50%	103.08%	20.42%	8.78%	2.80%	7.68%
100% CAD	07/31/17	77.00%	48.53%	28.47%	9.48%	4.23%	10.82%
Retirement CAD	07/31/18	28.21%	37.23%	-9.02%	4.72%	-4.93%	0.14%
Retirement USD	07/31/18	64.78%	73.53%	-8.75%	9.71%	2.84%	7.89%

*Canadian portfolios added value is calculated based on 50% of VIG and 50% of XDV as half of portfolios are US stocks. Currency hasn't been taken into consideration.

Benchmarks are VIG and XDV.TO for all portfolios.