cardinal UPDATE

MARCH 2015

DIVIDEND INCREASES

BCE Inc.	5.3%
CIBC	2.9%
Cisco Systems Inc.	10.5%
Great-West Lifeco. Inc.	6.0%
Nestlé	2.3%
Rio Tinto	12.0%
Royal Bank of Canada	2.7%
Toronto-Dominion Bank	8.5%
United Technologies Corp.	8.5%

(During the period: February 1 - 28, 2015)

A TIME TO DE-RISK

March 9th was supposedly a red-letter day for stock market aficionados. It marked the sixth anniversary of the current bull market, which started from the depths of the despair prevailing in the market melt-down following the Lehman Brothers bankruptcy in 2008 – the fourth longest bull market in recent US market history, and one that the media would argue might be ending soon. The media neglects the fact that the longest bull ran for 13 years, from 1987 to 2000, and also fails to remind us of how low markets dove in 2008. We could argue that 2008 was a much worse market event than 1987, and so the bull rise out of 2008 might be better than the bull rise out of 1987, but that is speculation.

What matters to us is the US economy continuing to strengthen and it is in no way at a level where the Federal Reserve needs to slow growth in order to quell inflation. We do expect that the Federal Reserve will want to increase interest rates to a "more normal" level, and would like to do that sooner rather than later, but they are not going to jeopardize the recovery which they have fostered through years of Quantitative Easing by raising rates too much, too soon.

In Canada on the other hand, we see growth slowing largely because of energy investments and public sector restraint. We at Cardinal have been busy doing a kind of market timing that we believe in – Looking for Value. You may have noticed that we divested Magna and Saputo from our Canadian portfolios (at considerable profit for most clients) and may also note that we invested the proceeds in some fairly conservative names – BCE, Telus, Sun Life and Empire Corp. We don't believe that markets are predictable, but we do hold strong opinions about when individual companies are trading well above fair value. The markets may still love Magna and Saputo, but if we feel they are overvalued, then we would rather seek other opportunities with less downside.

This shift from overvalued names to more undervalued ones is our way of de-risking the portfolio. While a market timer would go to cash, we instead look to reduce risk by investing in more conservative companies, generally with higher dividend yields than the stocks we sold. If the markets continue to move upwards, these stocks are likely to participate, but if economic weakness feeds into a market sell-off, these companies are likely to fare better than the market as a whole, and will still yield excellent dividend income for our clients. These trades did trigger capital gains for unregistered accounts. Our job is to grow and protect capital, not to indefinitely postpone tax. This is an opportune time to de-risk in Canada, and this is the kind of timing decision that our clients rely on us to make.

COMPANY FOCUS

CNQ

Dividends are not just a source of income in the form of a share of profits. An increasing dividend is an important signal of management's confidence in the future direction of the business. This is especially true in the oil patch right now. Not only are very few companies increasing dividends, but the decline in oil prices has caused companies with high payout ratios, over-leveraged balance sheets, and weaker operations to reduce their dividend. Quoting Warren Buffett, "Only when the tide goes out do you discover who's been swimming naked."

We were therefore quite pleased when on March 5th Canadian Natural Resources (CNQ) announced a 2.2% increase to their dividend, marking 15 consecutive years of dividend growth. The company's balance sheet, conservative payout ratio, and operations have never been better.

2015 will still be a tough year as cash flows fall, however, costs will be reduced on long-term projects and distressed competitors may offer up assets on the cheap. CNQ also has the option of selling its royalty assets to create greater financial flexibility. Today's tough market conditions create opportunities for strong companies like CNQ, and for their patient, long-term investors.

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