

High-Dividend Portfolio

Portfolio Manager Commentary

As of 12/31/2019



Q4 2019 Commentary

The **High-Dividend Portfolio (HDP)** posted another three months of positive absolute and relative performance in the fourth quarter of 2019 (4Q19) as strength in Financials and Consumer Discretionary positions more than offset weak performance in Real Estate Investment Trusts (REITs) and Energy. The surge in dividend stocks relative to growth stocks that had been very prevalent in the third quarter of 2019 abated some during the fourth quarter. Investor fears over a near-term recession were eased by stabilizing economic data and positive developments on trade—leading to an increased risk appetite. Still, the balanced nature of the portfolio, as demonstrated by a fairly even and intentional split between cyclical and defensive positions, allowed for solid gains even in the “risk on” environment.

Key Performance Highlights:

- ▶ HDP 4Q19 gross total return of 5.87% (5.78% net) exceeded the 4.54% benchmark return for the S&P 500 Low Volatility High Dividend Total Return Index (SP5LVHDT)
- ▶ Year-to-date HDP gross total return of 21.78% (21.36% net) also outpaced the 20.76% return for the SP5LVHDT
- ▶ Average dividend yield of the stocks within the portfolio ended the quarter at 5.49%

Key Investment Highlights:

We continue to believe that dividend yielding stocks will play a vital role in a “lower for longer” environment for interest rates, inflation, and GDP growth as investors put increasing emphasis on cash flow in a well-diversified investment portfolio. Specifically:

- ▶ **HDP generates a high level of current income primarily from investment grade companies.** The 5.49% average dividend yield represents a similar yield to that of a high-yield corporate bond portfolio while maintaining a much higher concentration in investment grade companies. On a weighted average basis, 81% of the stocks within the portfolio are investment grade. In addition, the average dividend increase within the portfolio was just under 5% in 2019, which more than covers the current inflation rate. (**Figure 1, page 2**)
- ▶ **High-dividend yielding stocks have outperformed over time.** Based on our analysis, high-dividend yielding stocks (yields greater than twice that of the S&P 500), have outperformed the S&P 500 as well as its non-dividend paying constituents over the past 30 years. The compounded annual growth rate (CAGR) of high-dividend yielding stocks is approximately 12.0% over the past 30 years versus 11.5% for the S&P 500 and just 11.0% for non-dividend paying stocks within the S&P 500.

Objective

Seeks to generate a high level of current income with dividend growth to cover inflation and a yield that is competitive with U.S. high-yield bond benchmarks

Portfolio Management Team



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About EquityCompass

EquityCompass is a Baltimore-based SEC registered investment adviser offering a broad range of portfolio strategies and custom plans for individuals, financial intermediaries, and institutional clients in the U.S. and Europe. Formally organized in 2008, EquityCompass provides portfolio strategies with respect to total assets of approximately \$4.3 billion as of December 31, 2019.*

The EquityCompass team of professionals represents deep industry experience in security analysis, capital markets, and portfolio management. We are committed to a consistent investment process that relies on enduring principles, sound empirical reasoning, and the recognition of a dynamic investment environment with a global reach.

	Total Returns			Annualized Returns		Calendar-Year Returns	
	3-Mos	6-Mos	YTD	1-yr	Inception	2018	2019
Gross %	5.87	9.90	21.78	21.78	8.90	-7.95	21.78
Net %	5.78	9.70	21.36	21.36	8.52	-8.27	21.36
SP5LVHDT %	4.54	7.11	20.76	20.76	8.69	-5.87	20.76
HFRISRE %	-0.20	-0.86	10.38	10.38	3.40	-4.33	10.38

Inception – September 1, 2017; Benchmark = S&P 500 Low Vol High Dividend (SP5LVHDT); HFRYield Alternatives (HFRISRE)

The information provided herein is supplemental to the GIPS performance presentation. To obtain a compliant presentation or a list of our composite descriptions and/or policies for valuing portfolios, calculating performance, and preparing compliant presentations, please call (443) 224-1231 or send an e-mail to info@equitycompass.com. Indices are unmanaged, do not reflect fees and expenses, and are not available for direct investment. Past performance does not guarantee future results.

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► **Risk mitigation through balance and diversification.** The portfolio consists of 30 stocks from 10 different industry sectors, with an average market cap of \$76.5 billion. In addition, the barbell approach we have taken with the portfolio construction provides exposure to high-dividend yielding stocks in both cyclical and defensive oriented industries. This balance is intended to position the portfolio in a diversified manner to withstand various economic environments. For example, in 4Q19, exposure to Financial and Consumer Discretionary sectors was the primary driver of the solid quarterly performance as near-term recession fears began to fade. Conversely, exposure to REITs and Utilities helped drive outperformance in the previous quarter.

We consider HDP a supplemental strategy to complement, not replace, core income-oriented investments with an allocation similar to that of a high yield corporate bond portfolio. The portfolio's primary goals are to provide: (1) a net cash flow yield in excess of 4% (net of fees) and (2) capital appreciation.

Yield and Investment Grade Comparison

Figure 1

Data as of 12/31/2019 | Source: Bloomberg Finance L.P., EquityCompass | Key: YTM = Yield to Maturity

		IBOXHY		HDP	
Bond Rating		Weight	Average YTM	Weight	Avg. Div Yld.
Investment Grade	AAA				
	AA			8.75%	5.05%
	A			23.79%	4.79%
	BBB	3.40%	3.89%	45.87%	5.63%
Non-Investment Grade	BB	51.92%	4.50%	15.98%	6.20%
	B	35.45%	5.89%		
	CCC and lower	8.15%	11.63%		
	Not Rated	0.82%	5.31%	2.72%	6.27%
	Cash	0.26%	0.00%	2.89%	0.00%
Weighted Average Yield			5.55%		5.33%
Total Inv. Grade & Cash		3.66%	3.89%	81.30%	5.31%
Total BB+ or lower		95.5%	5.62%	15.98%	6.20%
Total B+ or lower		43.6%	6.96%		
Total CCC+ or lower		8.2%	11.63%		
Debt to EBITDA		6.26		3.86	

DISCLOSURES

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*Total assets combines both Assets Under Management and Assets Under Advisement as of December 31, 2019. Assets Under Management represents the aggregate fair value of all discretionary and non-discretionary assets, including fee paying and non-fee paying portfolios. Assets Under Advisement represent advisory-only assets where the firm provides a model portfolio and does not have trading authority over the assets.

Securities discussed in this material were selected because they had dividend increases or decreases in the most recent period and not based on any measurement of performance of the underlying security. Any projections, targets, or estimates in this report are forward looking statements and are based on EquityCompass research, analysis, and assumptions made by the Adviser. Changes in market conditions or a company's financial condition may impact a company's ability to continue to pay dividends. Companies may also choose to discontinue dividend payments. Due to their narrow focus, sector-based investments typically exhibit greater volatility and are generally associated with a high degree of risk. Rebalancing may have tax consequences, which should be discussed with your tax advisor.

Strategy Specific Risks: Small company stocks are typically more volatile and carry additional risks, since smaller companies generally are not as well established as larger companies. The market risk associated with small-cap and mid-cap stocks is generally greater than that associated with large-cap stocks because small-cap and mid-cap stocks tend to experience sharper price fluctuations than large-cap stocks, particularly during bear markets. Due to their narrow focus, sector-based investments typically exhibit greater volatility and are generally associated with a high degree of risk. Changes in market conditions or a company's financial condition may impact the company's ability to continue to pay dividends. Companies may also choose to discontinue dividend payments. High-dividend paying stocks may carry elevated risks and companies may lower or discontinue dividends at any time.

Foreign investments are subject to risks not ordinarily associated with domestic investments, such as currency, economic and political risks, and different accounting standards. There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in emerging markets may involve greater risk and volatility than investing in more developed countries. Rebalancing may have tax consequences, which should be discussed with your tax advisor. Foreign securities potentially entail special risks such as less liquid markets; political and economic instability; lax regulation; and adverse fluctuations in currency exchange rates.

Real estate investing is subject to special risks, including tenant default, declining occupancy rates, adverse changes in environmental and zoning regulations, and falling property values and rents due to deteriorating local or national economic conditions. REIT securities listed on a securities exchange may be subject to abrupt or erratic price movements because of interest rate changes and other factors. Non-listed REIT securities may lack sufficient liquidity to enable the Fund to sell them at an advantageous time or to minimize a loss. Distributions from REITs may include a return of capital. A REIT that does not qualify as a REIT under the Internal Revenue Code ("IRC") will pay taxes on its earnings, which will reduce the dividends paid by the REIT to the Fund. Some REITs are highly leveraged, which may increase the risk of loss.

The S&P 500 Low Volatility High Dividend index measures the performance of the 50 least-volatile high dividend-yielding stocks in the S&P 500. The index is designed to serve as a benchmark for income-seeking investors in the U.S. equity market. HFRI Yield Alternatives Index is a fund-weighted index of select hedge funds that employ an investment thesis predicated on realization of a spread between related instruments in which one or multiple components of the spread contains a derivative, equity, real estate, MLP or combination of these or other instruments. Strategies employ an investment process designed to isolate opportunities in yield oriented securities, which can include equity, preferred, listed partnerships (MLPs), REITs and some other corporate obligations.

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