

# Favoured valuation metric drives search for U.S. dividend stocks

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## WHAT ARE WE LOOKING FOR?

My associate Allan Meyer and I seek out U.S. dividend payers using our investment philosophy focused on safety and value, this time highlighting one of our favourite valuation metrics, free-cash-flow-to-enterprise-value.

## THE SCREEN

We started with U.S.-listed equities in the S&P 500 index, which is composed of large-cap names. Market capitalization is a safety factor – larger companies tend to be more stable and diverse.

Dividend yield is the projected annualized dividend payments divided by the share price. Many of our clients love to get paid while they wait for capital appreciation and dividends generally

## Select S&P 500 dividend stocks

| COMPANY                      | TICKER | RECENT PRICE (US\$) | MARKET CAP. (US\$BIL) | DIV. YIELD (%) | DIV. PAYOUT RATIO (%) | DEBT/EQUITY (%) | FCF/EV (%)  | EARNINGS MOMENTUM (%) | 52WK TOTAL RTN (%) |
|------------------------------|--------|---------------------|-----------------------|----------------|-----------------------|-----------------|-------------|-----------------------|--------------------|
| Seagate Technology PLC       | STX-Q  | 47.57               | 13.2                  | 5.3            | 40.0                  | 289.4           | <b>12.1</b> | -10.2                 | -12.3              |
| LyondellBasell Industries NV | LYB-N  | 81.98               | 30.4                  | 4.9            | 36.0                  | 91.5            | <b>9.1</b>  | -7.9                  | -24.0              |
| Harley-Davidson Inc.         | HOG-N  | 35.95               | 5.7                   | 4.2            | 50.2                  | 428.4           | <b>8.4</b>  | -6.8                  | -8.1               |
| Macy's Inc.                  | M-N    | 22.70               | 7.0                   | 6.7            | 42.7                  | 73.8            | <b>8.4</b>  | -2.1                  | -19.0              |
| IBM                          | IBM-N  | 135.34              | 120.0                 | 4.8            | 53.1                  | 272.8           | <b>8.2</b>  | -1.4                  | -1.7               |
| Westrock Co.                 | WRK-N  | 37.15               | 9.5                   | 4.9            | 60.0                  | 55.9            | <b>8.2</b>  | -0.7                  | -36.1              |
| Gap Inc.                     | GPS-N  | 24.98               | 9.5                   | 4.0            | 44.5                  | 35.2            | <b>7.6</b>  | 4.4                   | -10.1              |
| Valero Energy Corp.          | VLO-N  | 81.74               | 34.1                  | 4.4            | 50.6                  | 42.0            | <b>7.4</b>  | -9.1                  | -26.1              |
| International Paper Co.      | IP-N   | 45.71               | 18.2                  | 4.4            | 46.1                  | 144.7           | <b>7.4</b>  | 3.2                   | -10.0              |
| AT&T Inc.                    | T-N    | 30.38               | 221.7                 | 6.7            | 77.8                  | 95.9            | <b>7.3</b>  | 0.3                   | 1.5                |
| Western Union Co.            | WU-N   | 19.20               | 8.3                   | 4.2            | 40.9                  | 0.0             | <b>7.1</b>  | -3.1                  | -0.3               |
| Altria Group Inc.            | MO-N   | 51.99               | 97.3                  | 6.2            | 88.9                  | 174.1           | <b>7.0</b>  | -1.3                  | -1.9               |
| Verizon Communications Inc.  | VZ-N   | 56.48               | 233.6                 | 4.3            | 61.6                  | 212.7           | <b>6.2</b>  | 0.6                   | 24.9               |

Source: Eikon & Wickham Investment Counsel Inc.

reflect safety and stability. All securities listed yield 4 per cent or more.

Dividend payout ratio is the dividend payment divided by earnings. A lower number is preferred and may foreshadow a future dividend hike. We've capped payout at 100 and anything above could signal the potential for a cut.

Debt-to-equity is our last safety measure. It is the debt outstanding divided by sharehol-

ders' equity. A smaller ratio indicates a company has lower levels of debt or leverage. As we like to tell our clients, it's difficult to go bankrupt without owing any debts.

And now to our valuation measure, free-cash-flow-to-enterprise-value (FCF/EV): FCF is the cash left over for investors after all expenses, reinvestments and capital expenditures, while EV is a measure of the company's value excluding its cash. The

higher the number, the better the value. All securities must have a FCF/EV of 6 per cent or better and our list is sorted on this metric, from highest to lowest.

We believe free cash flow is more difficult to manipulate compared with other accounting metrics such as earnings.

Earnings momentum is the change in annual earnings over the past quarter.

A positive number implies

earnings are increasing, and vice-versa for a negative number.

Lastly, we've provided the 52-week total return to track recent performance.

## WHAT WE FOUND

Gap Inc. and AT&T Inc. score well across the board for safety and value. AT&T is the highest yielding on our list, along with Macy's Inc., while Seagate Technology PLC boasts the best value according to FCF/EV. International Paper Co. and Verizon Communications Inc. also look interesting on most measures but the debt levels are on the high side.

Verizon and AT&T are the only names with positive share-price performance over the past year. They are also two of only four companies that showed positive earnings momentum over the past quarter – Gap and International Paper being the others.

Investors should contact an investment professional or conduct further research before buying any of the securities listed here.