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### **First Quarter 2010**

We report the return\* for the year-to-date and previous calendar years because January 1<sup>st</sup> is a consistent starting point that makes comparisons easy (and because the CFA Institute frowns on cherry picking beginning and ending dates). We also like to report trailing 12-month returns. They are featured in the media and we have all become conditioned to think in 12-month intervals. However, I caution you that rolling 12-month returns are very volatile. When thinking about rates of return it is important to remember that the starting point (in this case April 1, 2009) is as important as the end date. This quarter the starting point for the 12-month returns is not even one month off the depths of the financial crisis. The difference to 12 months ago is night and day. The stock market is known as the Temple of Regrets. Like the trailing 12-month returns, the regrets have flipped in the last year – from regretting not having sold more to regretting not having bought more.

I've always marveled at (and often hung these quarterly letters on) the capacity of the investment industry to invent new jargon to describe what's new. I can't resist sharing my current favourite. Following the popularization of "BRIC" (Brazil, Russia, India, and China) which I wrote about a few years ago and which encapsulated the emerging markets and commodities theme, "PIGS" (Portugal, Italy or Ireland, Greece, and Spain) became current last year. It captured the idea that sovereign credit default risk had become a preoccupation after the massive government spending in response to the economic crisis. But the new characterization is 'Club Med' countries, which was coined to express what is said to be the relaxed attitude of the governments of Portugal, Italy, Greece, and Spain to paying people back. After all, Greece, the world's particular focus this month, has been in default about half the time since it was created in 1827.

Squeezed into this page is a table we're calling the dividend watch. It lists a sampling of stocks that have announced increases to their dividends in just the last few months. A few times in the last couple of years I've described my overarching investment theme for equities as a focus on dividend growth.

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\* Rates of return are measured: on the consolidated portfolio on a time-weighted basis (which takes into account the date and the amount of additions and withdrawals from each account); are the total returns (including interest, dividends and price changes); are calculated in Canadian dollars; fees have been deducted.

Company	Dividend Notes	2009 Dividend per share (\$)	Indicated Dividend for 2010 (\$)	Current Dividend Yield
BCE Inc.	Raised their dividend 3 times in 2009 (19% total increase).	\$1.54	\$1.74	5.83%
Canadian National Railway	Increased every year since they went public in 1995.	\$1.01	\$1.08	1.75%
Coca Cola	7% increase. Increased for 48 years in a row.	\$1.64	\$1.76	3.20%
Colgate Palmolive	21% increase. 44 <sup>th</sup> consecutive annual increase.	\$1.76	\$2.12	2.49%
Enbridge Inc.	Over the past 10 years the dividend has increased an average of 10% each year.	\$1.48	\$1.70	3.51%
Fortis Inc.	37 <sup>th</sup> consecutive increase, the longest record of any public company in Canada.	\$1.04	\$1.12	3.88%
Intel Corp.	12.5% increase. Has increased from \$0.08 in year 2000.	\$0.56	\$0.63	2.80%
Pall Corp.	10% dividend increase, 6 <sup>th</sup> year in a row.	\$0.58	\$0.64	1.58%
Shaw Communications	Has increased the dividend every year since 2000.	\$0.83	\$0.88	4.38%
3M Company	Has paid every quarter since 1916 and have increased it for 52 years in a row.	\$2.04	\$2.10	2.50%
Thomson Reuters	17 <sup>th</sup> consecutive increase.	\$1.12	\$1.16	3.20%
TransCanada	10 <sup>th</sup> consecutive increase.	\$1.52	\$1.60	4.30%
Wal-Mart	11% increase. Up every year since the company went public in 1974.	\$1.09	\$1.21	2.18%

Source: Thomson Reuters

We have invested in many companies with a) substantial dividend yields, b) a history of growing dividends, and c) financial characteristics conducive to sustained dividend increases. This selection technique mitigates stock market risk because a) high yields support stock prices, b) cash coming into a portfolio increases the ability to buy low, and c) current income increases the ability to wait out low stock prices.

The longer term strategic considerations are that the demographics of much of the developed world – an aging population – argue for increasing demand for income, and preferably a rising income to offset inflation. Inflation is the easiest way for governments to reduce the value of their liabilities in real terms. Governments that don't default or inflate will eventually have to restrain spending and borrowing and raise taxes, or be faced with a buyer's strike against their bonds. After the huge gains in corporate bonds last year, and the pressure on government bond yields, I have difficulty foreseeing how to make much money in fixed income now. That still leaves liquidity and safety as two good reasons to own some fixed income however.

My 4-year old Matthew and I had great fun watching curling at the Olympics on TV this winter. We don't play the game but came to recognize some jargon. When skippers want a stone to move faster they encourage their sweepers by yelling "Hurray! Hurrrray!" When they want the stone to move slower they yell "Off. Offff!" It struck me that so it has been with financial markets. On days when the appetite for risk assets is turned on, traders Hurray! into oil, stocks, high yield bonds, and the Canadian dollar. On days when the risk trade is Off! the U.S. dollar is strong, and stocks and oil are weak. I really must try the game. This past winter the risk trade has been mostly on. Go Canada!

Sincerely,

George Stedman, CFA  
Portfolio Manager

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